SEP 2 1982

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ORIGINAL

97th Congress
2d Session
HOUSE OF REPRESENTATIVES
REPORT
No. 97-760

COMPLETED

TAX EQUITY AND FISCAL RESPONSIBILITY ACT OF 1982

CONFERENCE REPORT

TO ACCOMPANY

H.R. 4961

AUGUST 17, 1982.—Ordered to be printed

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U.S. GOVERNMENT PRINTING OFFICE
97-588 O WASHINGTON : 1982

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TAX EQUITY AND FISCAL RESPONSIBILITY ACT OF 1982

August 17, 1982.—Ordered to be printed

Mr. Rostenkowski, from the committee of conference,
submitted the following

CONFERENCE REPORT

[To accompany H.R. 4961]

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 4961) to make miscellaneous changes in the tax laws, and for other purposes, having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the House recede from its disagreement to the amendment of the Senate to the text of the bill and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

SECTION 1. SHORT TITLE; TABLE OF CONTENTS; AMENDMENT OF 1954 CODE.

(a) Short Title.—This Act may be cited as the "Tax Equity and Fiscal Responsibility Act of 1982".

(b) Table of Contents.—

Sec. 1. Short title; table of contents; amendment of 1954 Code.

TITLE I—PROVISIONS RELATING TO SAVINGS IN HEALTH AND INCOME SECURITY PROGRAMS

Subtitle A—Medicare

Part I—Changes in Payments for Services

Subpart A—Amount of Payment for Institutional Services

Sec. 101. Payment for inpatient hospital services.
Sec. 102. Single reimbursement limit for skilled nursing facilities.
Sec. 103. Elimination of inpatient routine nursing salary cost differential.
Sec. 104. Elimination of duplicate overhead payments for outpatient services.
Sec. 105. Single reimbursement limit for home health agencies.
Sec. 106. Prohibiting payment for Hill-Burton free care.
Sec. 107. Prohibiting payment for anti-unionization activities.

Sec. 108. Reimbursement of provider-based physicians.
Sec. 109. Prohibiting recognition of payments under certain percentage arrangements.
Sec. 110. Elimination of lesser-of-cost-or-charge provision.
Sec. 111. Elimination of private room subsidy.

Subpart B—Payments for Other Services

Sec. 112. Reimbursement for inpatient radiology and pathology services.
Sec. 113. Reimbursement for assistants at surgery.
Sec. 114. Payments to health maintenance organizations and competitive medical plans.
Sec. 115. Prohibition of payment for ineffective drugs.

Subpart C—Other Payment Provisions

Sec. 116. Medicare payments secondary for older workers covered under group health plans.
Sec. 117. Interest charges on overpayments and underpayments.
Sec. 118. Audit and medical claims review.
Sec. 119. Private sector review initiative.
Sec. 120. Temporary delay in periodic interim payments.

PART II—CHANGES IN BENEFITS, PREMIUMS, AND ENROLLMENT

Sec. 121. Medicare coverage of Federal employees.
Sec. 122. Hospice care.
Sec. 123. Coverage of extended care services without regard to three-day prior hospitalization requirement.
Sec. 124. Provision temporarily holding part B premium at constant percentage of cost.
Sec. 125. Special enrollment provisions for merchant seamen.

PART III—MISCELLANEOUS PROVISIONS

Sec. 126. Extending medicare proficiency examination authority.
Sec. 127. Regualtions regarding access to books and records.
Sec. 128. Technical corrections to Omnibus Budget Reconciliation Act of 1981.

Subtitle B—Medicaid

Sec. 131. Copayments by medicaid recipients.
Sec. 132. Modifications in lien provisions.
Sec. 133. Limitation on Federal financial participation in erroneous medical assistance expenditures.
Sec. 134. Medicaid coverage of home care for certain disabled children.
Sec. 135. Six-month moratorium on deregulation of skilled nursing and intermediate care facilities.
Sec. 136. Medicaid program in American Samoa.
Sec. 137. Technical corrections from Omnibus Budget Reconciliation Act of 1981.

Subtitle C—Utilization and Quality Control Peer Review

Sec. 141. Short title of subtitle.
Sec. 142. Requirement for Secretary to enter into contracts.
Sec. 143. Establishment of utilization and quality control peer review program.
Sec. 144. Facilitation of private review.
Sec. 145. Waiver of liability provision.
Sec. 146. Medicaid provisions.
Sec. 147. Demonstration projects for competitive bidding and other reimbursement methods.
Sec. 148. Technical amendments.
Sec. 149. Effective date.
Sec. 150. Maintenance of current PSRO agreements.

Subtitle D—Aid to Families with Dependent Children

Sec. 151. Rounding of eligibility and benefit amounts.
Sec. 152. Effective date of application; proration of first month's AFDC benefit.
Sec. 153. Absence from home solely by reason of uniformed service.
Sec. 154. Job search.
Sec. 155. Proration of standard amount for shelter and utilities.

Sec. 156. Limitation of Federal financial participation in erroneous assistance expenditures.
Sec. 157. Exclusion from income of certain State payments.
Sec. 158. Extension of time for States to establish a work incentive demonstration program.
Sec. 159. Exclusion from income.
Sec. 160. Technical amendments to social services and foster care provisions in 1981 reconciliation Act.
Sec. 161. Delayed effective date in cases requiring conforming State legislation.

Subtitle E—Child Support Enforcement

Sec. 171. Fee for services to non-AFDC families.
Sec. 172. Allotments from pay for child and spousal support owed by members of the uniformed services on actived duty.
Sec. 173. Reimbursement of State agency in initial month of ineligibility for AFDC.
Sec. 174. Reduction in certain Federal payments to States under child support enforcement program.
Sec. 175. Technical amendments to child support enforcement provisions in 1981 reconcilliation Act.
Sec. 176. Delayed effective date in cases requiring State legislation.

Subtitle F—Supplemental Security Income

Sec. 181. Effective date of application; proration of initial SSI benefit payment.
Sec. 182. Rounding of SSI eligibility and benefit amounts.
Sec. 183. Coordination of SSI and OASDI cost-of-living adjustments.
Sec. 184. Phaseout of hold harmless protection.
Sec. 185. Exclusion from resources of burial plots and certain funds set aside for burial expenses.
Sec. 186. Mandatory passthrough under State supplementation provisions.
Sec. 187. Treatment of unnegotiated checks under the supplemental security income program.

Subtitle G—Unemployment Compensation

Sec. 191. Rounding of benefit amounts.
Sec. 192. Use of certain amounts transferred to State unemployment funds.
Sec. 193. Treatment of certain employees of institutions of higher education.
Sec. 194. Short-time compensation.

TITLE II—REVENUE MEASURES

Subtitle A—Provisions Relating to Individuals

Sec. 201. Alternative minimum tax on taxpayers other than corporations.
Sec. 202. Limitation on medical deduction.
Sec. 203. Limitation on deduction for nonbusiness casualty losses.

Subtitle B--Provisions Primarily Relating to Business

Part I—Reduction in Certain Deductions and Credits

Sec. 204. 15 percent reduction in certain corporate preference items.
Sec. 205. Amendments to investment credit.
Sec. 206. Repeal of 1985 and 1986 increases in accelerated cost recovery deductions.
Sec. 207. Section 189 made applicable to certain corporations for nonresidential real property.

Part II—Leasing

Sec. 208. Limitations and additional requirements on leases under the accelerated cost recovery system.
Sec. 209. Repeal of leasing; special rule for leases with economic substance.
Sec. 210. Motor vehicle operating leases.

Part III—Foreign Tax

Sec. 211. Foreign tax credit for taxes on oil and gas income.
Sec. 212. Current taxation of foreign oil related income of controlled foreign corporations.
Sec. 213. Possession tax credit; income tax liability incurred to the Virgin Islands.

PART IV—TAX-EXEMPT OBLIGATIONS

Sec. 214. Modification of exemption for small issues.
Sec. 215. Public approval and information reporting requirements applicable to private activity bonds.
Sec. 216. Cost recovery for certain property financed with tax-exempt bonds.
Sec. 217. Miscellaneous.
Sec. 218. Treatment of certain refunding obligations.
Sec. 219. Limitation on maturity of industrial development bonds.
Sec. 220. Mortgage subsidy bonds.
Sec. 221. Industrial development bonds for certain residential rental property.

PART V—MERGERS AND ACQUISITIONS

Subpart A—Changes in Tax Treatment of Partial Liquidations and of Certain Distributions of Appreciated Property

Sec. 222. Partial liquidations.
Sec. 223. Distribution of appreciated property in redemption of stock.

Subpart B—Certain Stock Purchases Treated as Asset Purchases

Sec. 224. Certain stock purchases treated as asset purchases.

Subpart C—Miscellaneous Provisions

Sec. 225. Clarification of section 368(a)(1)(F).
Sec. 226. Amendments relating to bailouts through use of holding companies.
Sec. 227. Application of attribution rules for purposes of sections 306 and 356(a)(2).
Sec. 228. Waiver of family attribution by entities.

PART VI—METHODS OF ACCOUNTING

Sec. 229. Modification of regulations on the completed contract method of accounting.
Sec. 230. Annual accrual method of accounting extended to certain partnerships.

PART VII—ORIGINAL ISSUE DISCOUNT

Sec. 231. Original issue discount taken into account on basis of constant interest rate.
Sec. 232. Tax treatment of stripped bonds.

PART VIII—OTHER BUSINESS PROVISIONS

Sec. 233. Targeted jobs tax credit.
Sec. 234. Accelerated payment of income tax by corporations.

Subtitle C—Pensions

PART I—CONTRIBUTION AND LOAN LIMITS

Sec. 235. Lower contribution and benefit limits for certain annuities, etc.
Sec. 236. Loans treated as distributions.

PART II—REPEAL OF SPECIAL LIMITATIONS ON PLANS BENEFITING SELF-EMPLOYED INDIVIDUALS OR OWNER-EMPLOYEES

Sec. 237. Repeal of special qualification requirements.
Sec. 238. Repeal of special limitations on deduction for self-employed individuals and subchapter S corporations.
Sec. 239. Allowance of exclusion of death benefit for self-employed individuals.
Sec. 240. Special rules for top heavy plans.
Sec. 241. Effective dates.

PART III—OTHER REQUIREMENTS

Sec. 242. Required distributions for qualified plans.
Sec. 243. Required distributions in case of individual retirement plans.
Sec. 244. Limitation on exclusion for group-term life insurance purchased for employees.
Sec. 245. Limitation on estatae tax exclusions under section 2039.
Sec. 246. Organizations performing management functions.
Sec. 247. Existing personal service corporations may liquidate under section 333 during 1983 or 1984.

Sec. 248. Employee leasing.
Sec. 249. Nondiscriminatory coordination of defined contribution plans with OASDI.
Sec. 250. Authority of Secretary to allocate income and deductions in the case of certain corporations.

Part IV—Miscellaneous

Sec. 251. Church plans.
Sec. 252. Deferred compensation plans for State judges.
Sec. 253. Profit-sharing plan contributions on behalf of disabled.
Sec. 254. Exemption for trusts which include governmental plans.

Subtitle D—Taxation of Life Insurance Companies and Annuities

Part I—Coinsurance arrangements

Subpart A—Modified Coinsurance Contracts

Sec. 255. Repeal of optional treatment of policies reinsured under modified coinsurance contracts.
Sec. 256. Specialaccounting rules relating to repeal of section 820.

Subpart B—Other Reinsurance Agreements

Sec. 257. Denial of interest deduction on indebtedness incurred in connection with reinsurance agreements.
Sec. 258. Allocation of income, etc. in the case of other reinsurance agreements.

Part II—2-Year Temporary Provisions Relating to Taxation of Life Insurance Companies

Sec. 259. Increase in amount of dividend deduction allowed; pension plan reserves.
Sec. 260. Computation of amount of life insurance reserves.
Sec. 261. Modification of menge formula.
Sec. 262. Consolidated returns to be computed on a botton line basis.
Sec. 263. Effective dates; special rules applicable to transactions before effective date.

Part III—Excess Interest; Amounts Received Under Annuity Contracts; Computation of Reserves

Sec. 264. Allowance of deduction for excess interest.
Sec. 265. Treatment of amounts received and under annuity contracts before annuity starting date.
Sec. 266. Flexible premium contracts.
Sec. 267. Reduction in approximate revaluation method of computing reserves.

Part IV—Underpayments of Estimated Tax for 1982

Sec. 268. Underpayments of estimated tax for 1982.

Subtitle E—Employment Taxes

Part I—In General

Sec. 269. Treatment of real estate agents and direct sellers.
Sec. 270. Simplified procedure for determining amount of employment taxes.

Part II—Federal Unemployment Tax

Subpart A—Increase in Federal Unemployment Tax

Sec. 271. Increase in Federal unemployment tax wage base and rate.

Subpart B—Other Financing Provisions

Sec. 272. Credit reduction not to apply when State makes certain repayments.
Sec. 273. Limitation of fifth year credit reduction.
Sec. 274. Deferral of interest in case of certain States with high unemployment rates.
Sec. 275. Required repayments from extended unemployment compensation account.
Sec. 276. Treatment of certain services performed by students.
Sec. 277. Treatment of certain alien farm workers.

Part III—Medicare Coverage

Sec. 278. Medicare coverage of, and application of hospital insurance tax to, Federal employment.

Subtitle F—Excise Taxes

PART I—AIRPORT AND AIRWAY

Sec. 279. Tax on fuel used in noncommercial aviation.
Sec. 280. Tax on transportation by air.
Sec. 281. Extension of Airport and Airway Trust Fund.

PART II—COMMUNICATIONS SERVICES

Sec. 282. Extension of excise tax on communications services.

PART III—CIGARETTES

Sec. 283. Increase in tax on cigarettes.

PART IV—TAPS ADJUSTMENT ELIMINATED

Sec. 284. Elimination of the TAPS adjustment.

Subtitle G—Miscellaneous

Sec. 285. Two-year extension of exclusion from gross income of national research service awards.
Sec. 286. Special rules for certain amateur sports organizations.
Sec. 287. New Jersey general revenue sharing allocation.
Sec. 283. Illegal payments to government officials or employees.
Sec. 289. Debt management provisions.
Sec. 290. Jefferson County mental health center.
Sec. 291. Alaska native corporations.
Sec. 292. Awarding of costs and certain fees.
Sec. 293. Treatment of certain lending of finance businesses for purposes of the tax on personal holding companies.
Sec. 294. Additional refunds relating to repeal of excise tax on buses.

TITLE III—TAXPAYER COMPLIANCE

Subpart A—Withholding on Interest and Dividends

Sec. 301. Withholding on interest and dividends.
Sec. 302. Credit against tax.
Sec. 303. Returns regarding payments of dividends and payments of interest.
Sec. 304. Returns regarding payments of patronage dividends.
Sec. 305. Denial of deduction for certain taxes.
Sec. 306. Penalties.
Sec. 307. Conforming and clerical amendments.
Sec. 308. Effective dates; special rules.

Subtitle B—Improved Information Reporting

PART I—EXPANDED REPORTING

Sec. 309. Reporting of interest.
Sec. 310. Obligations required to be registered.
Sec. 311. Returns of brokers.
Sec. 312. Information reporting requirements for payments of remuneration for services and direct sales.
Sec. 313. State and local income tax refunds.
Sec. 314. Employer reporting with respect to tips.

PART II—PROVISIONS TO IMPROVE REPORTING GENERALLY

Sec. 315. Increased penalties for failure to file information return or to furnish statement.
Sec. 316. Increased in civil penalty on failure to supply identifying numbers.
Sec. 317. Extension of withholding to certain payments where identifying number not furnished or inaccurate.
Sec. 318. Minimum penalty for extended failure to file.
Sec. 319. Information returns.

Subtitle C—Abusive Tax Shelters, Etc.; Substantial Underpayments; False Documents; Frivolous Returns

PART I—ABUSIVE TAX SHELTERS, ETC.

Sec. 320. Penalty for promoting abusive tax shelters, etc.
Sec. 321. Action to enjoin promoters of abusive tax shelters, etc.
Sec. 322. Procedural rules applicable to penalties under sections 6700, 6701 and 6702.

PART II—SUBSTANTIAL UNDERPAYMENT; FALSE DOCUMENTS; FRIVOLOUS RETURNS; ETC.

Sec. 323. Penalty for substantial understatement.
Sec. 324. Penalties for documents understating tax liability.
Sec. 325. Fraud penalty.
Sec. 326. Penalty for frivolous returns.
Sec. 327. Relief from criminal penalty for failure to file estimated tax where taxpayer falls within statutory exceptions.
Sec. 328. Adjustments to estimated tax provisions.
Sec. 329. Increases in certain criminal fines.
Sec. 330. Special rules with respect to certain cash.

Subtitle D—Administrative Summons

Sec. 331. Special procedures for third-party summons.
Sec. 332. Duty of third-party recordkeeper.
Sec. 333. Limitation on use of administrative summons.

Subtitle E—Withholding on Pensions and Other Retirement Income

Sec. 334. Withholding on pensions annuities, and certain other deferred income.
Sec. 335. Partial rollovers of IRA distributions permitted.

Subtitle F—Transactions Outside the United States or Involving Foreign Persons

Sec. 336. Jurisdiction of court and enforcement of summons in case of persons residing outside the United States.
Sec. 337. Admissibility of evidence maintained in foreign countries.
Sec. 338. Penalty for failure to furnish information with respect to certain foreign corporations.
Sec. 339. Information requirements with respect to certain foreign-owned corporations.
Sec. 340. Returns with respect to foreign personal holding companies.
Sec. 341. Authority to delay date for filing certain returns relating to foreign corporations and foreign trusts.
Sec. 342. Withholding of tax on nonresident aliens and foreign corporations.
Sec. 343. Technical amendment relating to penalty under section 905(c).

Subtitle G—Modification of Interest Provisions

Sec. 344. Interest compounded daily.
Sec. 345. Determination of rate of interest to be made semiannually.
Sec. 346. Restrictions on payment of interest for certain periods.

Subtitle H—Taxpayer Safeguard Amendments

Sec. 347. Increase in certain exemptions from levy.
Sec. 348. Required release of lien.
Sec. 349. Requirement of timely notice of levy.
Sec. 350. Amount of damages in case of wrongful levy.

Subtitle I—Other Provisions

Sec. 351. Disallowance of deductions relating to narcotics trafficking.
Sec. 352. Sense of Congress with respect to providing of additional funds to Internal Revenue Service.
Sec. 353. Report on forms.
Sec. 354. Exemption of veterans' organizations.
Sec. 355. Amendment to Communications Act of 1934.
Sec. 356. Confidentiality and disclosure of returns and return information.
Sec. 357. Civil damages against United States for unauthorized disclosures by an employee.
Sec. 358. Disclosure for use in certain audits by General Accounting Office.

TITLE IV—TAX TREATMENT OF PARTNERSHIP ITEMS

Sec. 401. Short title.
Sec. 402. Tax treatment of partnership items.
Sec. 403. Requirement that statement be furnished to partner.
Sec. 404. Returns required from all partnerships with United States partners.
Sec. 405. Return requirement for United States persons having interest in foreign partnerships.
Sec. 406. Special rule for certain international satellite partnerships.

TITLE V—AIRPORT AND AIRWAY IMPROVEMENT

Sec. 501. Short title.
Sec. 502. Declaration of policy.
Sec. 503. Definitions.
Sec. 504. National airport and airway system plans.
Sec. 505. Airport improvement program.
Sec. 506. Airway improvement program.
Sec. 507. Apportionment of funds.
Sec. 508. Use of apportioned and discretionary funds; miscellaneous conditions.
Sec. 509. Submission and approval of project grant applications.
Sec. 510. United States share of project costs.
Sec. 511. Project sponsorship.
Sec. 512. Grant agreements.
Sec. 513. Project costs.
Sec. 514. Payments under grant agreements.
Sec. 515. Performance of construction work.
Sec. 516. Use of Government-owned lands.
Sec. 517. False statements.
Sec. 518. Access to records.
Sec. 519. General powers.
Sec. 520. Civil rights.
Sec. 521. Reports to Congress.
Sec. 522. Report on ability of airports to finance airport development needs.
Sec. 523. Repeals; effective date; saving provisions; and separability.
Sec. 524. Miscellaneous amendments.
Sec. 525. Safety certification of airports.
Sec. 526. Contracting authority.
Sec. 527. Study of airport access.
Sec. 528. Part-time operation of flight service stations.
Sec. 529. Explosive detection K-9 teams.
Sec. 530. Release of certain conditions.
Sec. 531. Continuation of certain certificates.
Sec. 532. State taxation.

TITLE VI—FEDERAL SUPPLEMENTAL COMPENSATION PROGRAM

Subtitle A—Extension of Benefits

Sec. 601. Short title.
Sec. 602. Federal-State agreements.
Sec. 603. Payments to States having agreements for the payment of Federal supplemental compensation.
Sec. 604. Financing provisions.
Sec. 605. Definitions.
Sec. 606. Fraud and overpayments.

Subtitle B—Taxation of Unemployed Compensation

Sec. 611. Taxation of unemployment compensation.

(c) AMENDMENT OF 1954 CODE.—Except as otherwise expressly provided, whenever in titles II, III, and IV an amendment or repeal is expressed in terms of an amendment to, or repeal of, a section or other provision, the reference shall be considered to be made to a section or other provision of the Internal Revenue Code of 1954.

TITLE I—PROVISIONS RELATING TO SAVINGS IN HEALTH AND INCOME SECURITY PROGRAMS

Subtitle A—Medicare

PART I—CHANGES IN PAYMENTS FOR SERVICES

Subpart A—Amount of Payment for Institutional Services

PAYMENT FOR INPATIENT HOSPITAL SERVICES

SEC. 101. (a)(1) Title XVIII of the Social Security Act is amended by adding at the end thereof the following new section:

"PAYMENT TO HOSPITALS FOR INPATIENT HOSPITAL SERVICES

"SEC. 1886. (a)(1)(A)(i) The Secretary, in determining the amount of the payments that may be made under this title with respect to operating costs of inpatient hospital services (as defined in paragraph (4)) shall not recognize as reasonable (in the efficient delivery of health services) costs for the provision of such services by a hospital for a cost reporting period to the extent such costs exceed the applicable percentage (as determined under clause (ii)) of the average of such costs for all hospitals in the same grouping as such hospital for comparable time periods.

"(ii) For purposes of clause (i), the applicable percentage for hospital cost reporting periods beginning—

"(I) on or after October 1, 1982, and before October 1, 1983, is 120 percent;

"(II) on or after October 1, 1983, and before October 1, 1984, is 115 percent; and

"(III) on or after October 1, 1984, is 110 percent.

"(B)(i) For purposes of subparagraph (A) the Secretary shall establish case mix indexes for all short-term hospitals, and shall set limits for each hospital based upon the general mix of types of medical cases with respect to which such hospital provides services for which payment may be made under this title.

"(ii) The Secretary shall set such limits for a cost reporting period of a hospital—

"(I) by updating available data for a previous period to the immediate preceding cost reporting period by the estimated average rate of change of hospital costs industry-wide, and

"(II) by projecting for the cost reporting period by the applicable percentage increase (as defined in subsection (b)(3)(B)).

"(C) The limitation established under subparagraph (A) for any hospital shall in no event be lower than the allowable operating costs of inpatient hospital services (as defined in paragraph (4)) recognized under this title for such hospital for such hospital's last cost reporting period prior to the hospital's first cost reporting period for which this section is in effect.

"(2) The Secretary shall provide for such exemptions from, and exceptions and adjustments to, the limitation established under paragraph (1)(A) as he deems appropriate, including those which he deems necessary to take into account—

"(A) the special needs of sole community hospitals, of new hospitals, of risk based health maintenance organizations, and of hospitals which provide atypical services or essential community services, and to take into account extraordinary circumstances beyond the hospital's control, medical and paramedical education costs, significantly fluctuating population in the service area of the hospital, and unusual labor costs,

"(B) the special needs of psychiatric hospitals and of public or other hospitals that serve a significantly disportionate number of patients who have low income or are entitled to benefits under part A of this title, and

"(C) a decrease in the inpatient hospital services that a hospital provides and that are customarily provided directly by similar hospitals which results in a significant distortion in the operating costs of inpatient hospital services.

"(3) The limitation established under paragraph (1)(A) shall not apply with respect to any hospital which—

"(A) is located outside of a standard metropolitan statistical area, and

"(B)(i) has less than 50 beds, and

"(ii) was in operation and had less than 50 beds on the date of the enactment of this section.

"(4) For purposes of this section, the term 'operating costs of inpatient hospital services' includes all routine operating costs, ancillary service operating costs, and special care unit operating costs with respect to inpatient hospital services and such costs are determined on an average per admission or per discharge basis (as determined by the Secretary).

"(b)(1) Notwithstanding sections 1814(b) but subject to the provisions of sections 1813, if the operating costs of inpatient hospital services (as defined in subsection (a)(4)) of a hospital for a cost reporting period subject to this paragraph—

"(A) are less than or equal to the target amount (as defined in paragraph (3)) for that hospital for that period, the amount of the payment with respect to such operating costs payable under part A on a per discharge or per admission basis (as the case may be) shall be equal to the amount of such operating costs, plus—

"(i) 50 percent of the amount by which the target amount exceeds the amount of the operating costs, or

"(ii) 5 percent of the target amount,

whichever is less; or

"(B) are greater than the target amount, the amount of the payment with respect to such operating costs payable under part A on a per discharge or per admission basis (as the case may be) shall be equal to (i) the target amount, plus (ii) in the case of cost reporting periods beginning on or after October 1, 1982, and before October 1, 1984, 25 percent of the amount by which the amount of the operating costs exceeds the target amount;

except that in no case may the amount payable under this title with respect to operating costs of inpatient hospital services exceed the maximum amount payable with respect to such costs pursuant to subsection (a).

"(2) Paragraph (1) shall not apply to cost reporting periods of hospitals beginning on or after October 1, 1985.

"(3)(A) For purposes of this subsection, the term 'target amount' means, with respect to a hospital for a particular 12-month cost reporting period—

"(i) in the case of the first such reporting period for which this subsection is in effect, the allowable operating costs of inpatient hospital services (as defined in subsection (a)(4)) recognized under this title for such hospital for the preceding 12-month cost reporting period, and

"(ii) in the case a later reporting period, the target amount for the preceding 12-month cost reporting period,

increased by the applicable percentage increase under subparagraph (B) for that particular cost reporting period.

"(B) For purposes of subparagraph (A), the 'applicable percentage increase' for any 12-month cost reporting period shall be equal to 1 percentage point plus the percentage, estimated by the Secretary, by which the cost of the mix of goods and services (including personnel costs but excluding non-operating costs) comprising routine, ancillary, and special care unit inpatient hospital services, based on an index of appropriately weighted indicators of changes in wages and prices which are representative of the mix of goods and services included in such inpatient hospital services, for such cost reporting period exceeds the cost of such mix of goods and services for the preceding 12-month cost reporting period.

"(4)(A) The Secretary shall provide for an exemption from, or an exception and adjustment to, the method under this subsection for determining the amount of payment to a hospital where events beyond the hospital's control or extraordinary circumstances, including changes in the case mix of such hospital, create a distortion in the increase in costs for a cost reporting period (including any distortion in the costs for the base period against which such increase is measured). The Secretary may provide for such other exemptions from, and exceptions and adjustments to, such method as the Secretary deems appropriate, including those which he deems necessary to take into account a decrease in the inpatient hospital services that a hospital provides and that are customarily provided directly by similar hospitals which results in a significant distortion in the operating costs of inpatient hospital services.

"(B) Paragraph (1) shall not apply to payment of hospitals which is otherwise determined under paragraph (3) of section 1814(b).

"(5) In the case of any hospital having any cost reporting period of other than a 12-month period, the Secretary shall determine the 12-month period which shall be used for purposes of this section.

"(6)(A) The Secretary shall provide for an adjustment under this paragraph in the amount of payment otherwise provided a hospital under this subsection in the case of a hospital which, as of August 15, 1982, was subject to the taxes (hereinafter in this paragraph referred to as the 'FICA taxes') imposed by section 3111 of the Internal Revenue Code of 1954 and which is not subject to such taxes for part or all of a cost reporting period beginning on or after October 1, 1982.

"(B) In making such adjustment for a cost reporting period the Secretary shall estimate the amount of the operating costs of inpa-

tient hospital services that would have resulted if the hospital was subject to the FICA taxes during that period. In making such estimate the Secretary shall reduce the amount of such FICA taxes that would have been paid (but not below zero) by the amount of costs which the hospital demonstrates to the satisfaction of the Secretary were incurred in the period for pensions, health, and other fringe benefits for employees (and former employees and family members) comparable to, and in lieu of, the benefits provided under title II and this title of the Social Security Act.

"(C) If a hospital's operating costs of inpatient hospital services estimated under subparagraph (B) is greater than the hospital's operating costs of inpatient hospital services determined without regard to this paragraph for a cost reporting period, then the Secretary shall reduce the amount otherwise paid the hospital (respecting operating costs of inpatient hospital services) under this subsection for the period by the amount by which—

"(i) the amount that would have been paid the hospital if (I) the amount of the operating costs of inpatient hospital services estimated under subparagraph (B) were the treated as the amount of the operating costs of inpatient hospital services and (II) subsection (a) did not apply to the determination,

exceeds—

"(ii) the amount that would otherwise have been paid the hospital if subsection (a) (and this paragraph) did not apply;

except that, in making such determination for cost reporting periods beginning on or after October 1, 1984, clause (ii) of paragraph (1)(B) shall continue to apply.

"(c)(1) The Secretary may provide, in his discretion, that payment with respect to services provided by a hospital in a State may be made in accordance with a hospital reimbursement control system in a State, rather than in accordance with the other provisions of this title, if the chief executive officer of the State requests such treatment and if—

"(A) the Secretary determines that the system, if approved under this subsection, will apply (i) to substantially all nonfederal acute care hospitals (as defined by the Secretary) in the State and (ii) to the review of at least 75 percent of all revenues or expenses in the State for inpatient hospital services and of revenues or expenses for inpatient hospital services provided under the State's plan approved under title XIX;

"(B) the Secretary has been provided satisfactory assurances as to the equitable treatment under the system of all entities (including Federal and State programs) that pay hospitals for inpatient hospital services, of hospital employees, and of hospital patients; and

"(C) the Secretary has been provided satisfactory assurances that under the system, over 36-month periods (the first such period beginning with the first month in which this subsection applies to that system in the State), the amount of payments made under this title under such system will not exceed the amount of payments which would otherwise have been made under this title not using such system.

"(2) In determining under paragraph (1)(C) the amount of payment which would otherwise have been made under this title for a

State, the Secretary may provide for appropriate adjustment of such amount to take into account previous reductions effected in the amount of payments made under this title in the State due to the operation of the hospital reimbursement control system in the State if the system has resulted in an aggregate rate of increase in operating costs of inpatient hospital services (as defined in subsection (a)(4)) under this title for hospitals in the State which is less than the aggregate rate of increase in such costs under this title for hospitals in the United States.

"(3) The Secretary shall discontinue payments under a system described in paragraph (1) if the Secretary—

"(A) determines that the system no longer meets the requirement of paragraph (1)(A) or

"(B) has reason to believe that the assurances described in subparagraph (B) or (C) of paragraph (1) are not being (or will not be) met.".

(2) Section 1861(v)(1)(L) of such Act is amended by striking out "(i)" and all that follows through "(ii)".

(b)(1) The amendments made by subsection (a) shall apply to cost reporting periods beginning on or after October 1, 1982.

(2)(A) The Secretary of Health and Human Services shall first issue such final regulations (whether on an interim or other basis) before October 1, 1982, as may be necessary to implement such amendments on a timely basis. If such regulations are promulgated on an interim final basis, the Secretary shall take such steps as may be necessary to provide opportunity for public comment, and appropriate revision based thereon, so as to provide that such regulations are not on an interim basis later than March 31, 1983.

(B) Chapter 35 of title 5, United States Code, shall not apply, until January 1, 1984, to collection of information and information collection requests which the Secretary of Health and Human Services determines to be necessary to carry out the amendments made by this section.

(3) Section 1135 of the Social Security Act is amended by adding at the end the following new subsection:

"(c) The Secretary shall develop, in consultation with the Senate Committee on Finance and the Committee on Ways and Means of the House of Representatives, proposals for legislation which would provide that hospitals, skilled nursing facilities, and, to the extent feasible, other providers, would be reimbursed under title XVIII of this Act on a prospective basis. The Secretary shall report such proposals to such committees not later than December 31, 1982.".

(c)(1) Section 1814(b) of the Social Security Act is amended—

(A) by striking out "section 1813" in the matter before paragraph (1) and inserting in lieu thereof "sections 1813 and 1886"; and

(B) by striking out "until the Secretary determines" in the second sentence and inserting in lieu thereof "until the first day of the seventh month beginning after the date the Secretary determines and notifies the Governor of the State".

(2) Section 1833(a)(2)(B) of such Act is amended by inserting "and except as may be provided in section 1886" after "except those described in subparagraph (C) of this paragraph".

(d) Section 1861(v)(7) of such Act is amended by inserting "(A)" after "(7)" and by adding at the end thereof the following new subparagraph:

"(B) For further limitations on reasonable cost and determination of payment amounts for operating costs of inpatient hospital services and waivers for certain States, see section 1886.".

SINGLE REIMBURSEMENT LIMIT FOR SKILLED NURSING FACILITIES

SEC. 102. (a) Section 1861(v)(1) of the Social Security Act is amended—

(1) in subparagraph (E), by striking out "; except that" and all that follows and inserting in lieu thereof a period;

(2) in subparagraph (E), by striking out "(E)" and inserting in lieu thereof "(ii)"; and

(3) by inserting after subparagraph (D) the following:

"(E)(i) Such regulations shall provide that any determination of reasonable cost with respect to services provided by hospital-based skilled nursing facilities shall be made on the basis of a single standard based on the reasonableness of costs incurred by free standing skilled nursing facilities, subject to such adjustments as the Secretary may deem appropriate.".

(b) The amendment made by subsection (a) shall be effective with respect to cost reporting periods beginning on or after October 1, 1982.

ELIMINATION OF INPATIENT ROUTINE NURSING SALARY COST DIFFERENTIAL

SEC. 103. (a) Subparagraph (J) of section 1861(v)(1) of the Social Security Act is amended to read as follows:

"(J) Such regulations may not provide for any inpatient routine salary cost differential as a reimbursable cost for hospitals and skilled nursing facilities.".

(b) The amendment made by subsection (a) shall be effective with respect to cost reporting periods ending after September 30, 1982, but in the case of any cost reporting period beginning before October 1, 1982, any reduction in payments under title XVIII of the Social Security Act to a hospital or skilled nursing facility resulting from such amendment shall be imposed only in proportion to the part of the period which occurs after September 30, 1982.

ELIMINATION OF DUPLICATE OVERHEAD PAYMENTS FOR OUTPATIENT SERVICES

SEC. 104. (a) The last sentence of section 1842(b)(3) of the Social Security Act is amended by inserting after "1861(v)(1)(K)" the following: ", and in determining the reasonable charge for such services, the Secretary may limit such reasonable charge to a percentage of the amount of the prevailing charge for similar services furnished in a physician's office, taking into account the extent to which overhead costs associated with such outpatient services have been included in the reasonable cost or charge of the facility".

(b) The amendment made by subsection (a) made by this section shall be effective with respect to services furnished on or after October 1, 1982.

SINGLE REIMBURSEMENT LIMIT FOR HOME HEALTH AGENCIES

SEC. 105. (a) Section 1861(v)(1)(L) of the Social Security Act, as amended by section 101(a)(2) of this subtitle, is amended by inserting "free standing" after "75th percentile of such costs per visit for".

(b) The amendment made by subsection (a) shall be effective with respect to cost reporting periods beginning on or after the date of the enactment of this Act.

PROHIBITING PAYMENT FOR HILL-BURTON FREE CARE

SEC. 106. (a) Section 1861(v)(1) of the Social Security Act is amended by adding at the end the following new subparagraph:

"(M) Such regulations shall provide that costs respecting care provided by a provider of services, pursuant to an assurance under title VI or XVI of the Public Health Service Act that the provider will make available a reasonable volume of services to persons unable to pay therefor, shall not be allowable as reasonable costs.".

(b) The amendment made by subsection (a) shall be effective with respect to any costs incurred under title XVIII of the Social Security Act, except that it shall not apply to costs which have been allowed prior to the date of the enactment of this Act pursuant to the final court order affirmed by a United States Court of Appeals.

PROHIBITING PAYMENT FOR ANTI-UNIONIZATION ACTIVITIES

SEC. 107. (a) Section 1861(v)(1) of the Social Security Act, as amended by section 106(a) of this subtitle, is further amended by adding after subparagraph (M) the following new subparagraph:

"(N) In determining such reasonable costs, costs incurred for activities directly related to influencing employees respecting unionization may not be included.".

(b) The amendment made by subsection (a) shall be effective with respect to costs incurred after the date of the enactment of this Act.

REIMBURSEMENT OF PROVIDER-BASED PHYSICIANS

SEC. 108. (a) Title XVIII of the Social Security Act is amended by adding after section 1886 of the Social Security Act (as added by section 101(a)(1) of this subtitle) the following new section:

"PAYMENT OF PROVIDER-BASED PHYSICIANS

"SEC. 1887. (a)(1) The Secretary shall by regulation determine criteria for distinguishing those services (including inpatient and outpatient services) rendered in hospitals or skilled nursing facilities—

> *"(A) which constitute professional medical services, which are personally rendered for an individual patient by a physician and which contribute to the diagnosis or treatment of an individual patient, and which may be reimbursed as physicians' services under part B, and*

"(B) which constitute professional services which are rendered for the general benefit to patients in a hospital or skilled nursing facility and which may be reimbursed only on a reasonable cost basis.

"(2)(A) For purposes of cost reimbursement, the Secretary shall recognize as a reasonable cost of a hospital or skilled nursing facility only that portion of the costs attributable to services rendered by a physician in such hospital or facility which are services described in paragraph (1)(B), apportioned on the basis of the amount of time actually spent by such physician rendering such services.

"(B) In determining the amount of the payments which may be made with respect to services described in paragraph (1)(B), after apportioning costs as required by subparagraph (A), the Secretary may not recognize as reasonable (in the efficient delivery of health services) such portion of the provider's costs for such services to the extent that such costs exceed the reasonable compensation equivalent for such services. The reasonable compensation equivalent for any service shall be established by the Secretary in regulations.

"(C) The Secretary may, upon a showing by a hospital or facility that it is unable to recruit or maintain an adequate number of physicians for the hospital or facility on account of the reimbursement limits established under this subsection, grant exceptions to such reimbursement limits as may be necessary to allow such provider to provide a compensation level sufficient to provide adequate physician services in such hospital or facility.".

(2) Section 1861(v)(7) of such Act, as amended by section 101(d) of this subtitle, is further amended by adding at the end the following new subparagraph:

"(C) For provisions restricting payment for provider-based physicians' services, see section 1887.".

(c) The Secretary of Health and Human Services shall first promulgate regulations to carry out section 1887(a) of the Social Security Act not later than October 1, 1982. Such regulations shall become effective on October 1, 1982, and shall be effective with respect to cost reporting periods ending after September 30, 1982, but in the case of any cost reporting period beginning before October 1, 1982, any reduction in payments under title XVIII of the Social Security Act to a hospital or skilled nursing facility resulting from the such regulations shall be imposed only in proportion to the part of the period which occurs after September 30, 1982.

PROHIBITING RECOGNITION OF PAYMENTS UNDER CERTAIN PERCENTAGE ARRANGEMENTS

SEC. 109. (a) Section 1887 of the Social Security Act (as added by section 108(a) of this subtitle) is amended—

(1) by inserting "AND PAYMENT UNDER CERTAIN PERCENTAGE ARRANGEMENTS" at the end of its heading, and

(2) by adding at the end the following new subsection:

"(b)(1) Except as provided in paragraph (2), in the case of a provider of services which is paid under this title on a reasonable cost basis, or other basis related to costs that are reasonable, and which has entered into a contract for the purpose of having services furnished for or on behalf of it, the Secretary may not include any cost

incurred by the provider under the contract if the amount payable under the contract by the provider for that cost is determined on the basis of a percentage (or other proportion) of the provider's charges, revenues, or claim for reimbursement.

"(2) Paragraph (1) shall not apply—

"(A) to services furnished by a physician and described in subsection (a)(1)(B) and covered by regulations in effect under subsection (a), and

"(B) under regulations established by the Secretary, where the amount involved under the percentage contract is reasonable and the contract—

"(i) is a customary commerical business practice, or

"(ii) provides incentives for the efficient and economical operation of the provider of services.".

(b)(1) Section 1861(v)(1)(H)(iii) of such Act is amended by striking out "(I)" and by striking out ", or (II)" and all that follows through "furnished by the agency".

(2) Section 1861(v)(7)(C) of such Act, as added by section 108(b)(2) of this subtitle, is further amended by inserting "and for payments under certain percentage arrangements" after "services".

(c)(1) The amendments made by this section shall become effective on the date of the enactment of this Act, except that section 1887(b)(1) of the Social Security Act shall not apply before October 1, 1982, to services furnished by a physician and described in section 1887(a)(1)(B) of such Act.

(2) In the case of a contract with a provider of services entered into prior to the date of the enactment of this Act, the amendment made by subsection (a) shall apply to payments under such contract (A) 30 days after the first date (after such date of enactment) the provider of services may unilaterally terminate the contract, or (B) one year after the date of the enactment of this Act, whichever is earlier.

(3) The amendment made by subsection (b)(1) shall not apply to contracts entered into before the date of the enactment of this Act.

ELIMINATION OF LESSER-OF-COST-OR-CHARGE PROVISION

SEC. 110. Section 1886 of the Social Security Act, as added by section 101(a)(1) of this subtitle, is amended by adding at the end the following new subsection:

"(d)(1) The lesser-of-cost-or-charges provisions (described in paragraph (2)) will not apply in the case of services provided by a class of provider of services if the Secretary determines and certifies to Congress that the failure of such provisions to apply to the services provided by that class of providers will not result in any increase in the amount of payments made for those services under this title. Such change will take effect with respect to services furnished, or cost reporting periods of providers, on or after such date as the Secretary shall provide in the certification. Such change for a class of provider shall be discontinued if the Secretary determines and notifies Congress that such change has resulted in an increase in the amount of payments made under this title for services provided by that class of provider.

"(2) The lesser-of-cost-or-charges provisions referred to in paragraph (1) are as follows:

"(A) Clause (B) of paragraph (1) and paragraph (2) of section 1814(b).

"(B) So much of subparagraph (A) of section 1833(a)(2) as provides for payment other than of the reasonable cost of such services, as determined under section 1861(v).

"(C) Subclause (II) of clause (i) and clause (ii) of section 1833(a)(2)(B).".

ELIMINATION OF PRIVATE ROOM SUBSIDY

SEC. 111. (a) The Secretary of Health and Human Services shall, pursuant to section 1861(v)(2) of the Social Security Act, not allow as a reasonable cost the estimated amount by which the costs incurred by a hospital or skilled nursing facility for nonmedically necessary private accommodations for medicare beneficiaries exceeds the costs which would have been incurred by such hospital or facility for semiprivate accommodations.

(b) The Secretary of Health and Human Services shall first issue such final regulations (whether on an interim or other basis) as may be necessary to implement subsection (a) by October 1, 1982. If such regulations are promulgated on an interim final basis, the Secretary shall take such steps as may be necessary to provide opportunity for public comment, and appropriate revision based thereon, so as to provide that such regulations are not on an interim basis later than January 31, 1983.

Subpart B—Payments for Other Services

REIMBURSEMENT FOR INPATIENT RADIOLOGY AND PATHOLOGY SERVICES

SEC. 112. (a) Section 1833(a)(1) of the Social Security Act is amended—

(1) by striking out clause (B) and inserting in lieu thereof the following: "(B) with respect to items and services described in section 1861(s)(10), the amounts paid shall be 100 percent of the reasonable charges for such items and services,";

(2) by inserting "and" at the end of clause (F); and

(3) by striking out "and (H)" and all that follows through "for such items and services,".

(b) Clause (1) of section 1833(b) of such Act is amended to read as follows: "(1) such total amount shall not include expenses incurred for items and services described in section 1861(s)(10),".

(c) The amendments made by this section shall apply with respect to items and services furnished on or after October 1, 1982.

REIMBURSEMENT FOR ASSISTANTS AT SURGERY

SEC. 113. (a) Section 1842(b)(6) of the Social Security Act is amended by adding at the end thereof the following new subparagraph:

"(D)(i) In the case of physicians' services furnished to a patient in a hospital with a teaching program approved as specified in section 1861(b)(6) but which does not meet the conditions described in sec-

tion 1861(b)(7), no payment shall be made under this part for services of assistants at surgery with respect to a surgical procedure if such hospital has a training program relating to the medical specialty required for such surgical procedure and a qualified individual on the staff of the hospital is available to provide such services; except that payment may be made under this part for such services, to the extent that such payment is otherwise allowed under this paragraph, if such services, as determined under regulations of the Secretary—

"(I) are required due to exceptional medical circumstances,

"(II) are performed by team physicians needed to perform complex medical procedures, or

"(III) constitute concurrent medical care relating to a medical condition which requires the presence of, and active care by, a physician of another specialty during surgery,

and under such other circumstances as the Secretary determines by regulation to be appropriate.

"(ii) For purposes of this subparagraph, the term 'assistant at surgery' means a physician who actively assists the physician in charge of a case in performing a surgical procedure.

"(iii) The Secretary shall determine appropriate methods of reimbursement of assistants at surgery where such services are reimbursable under this part.".

(b) (1) The amendment made by subsection (a) is effective with respect to services performed on or after October 1, 1982.

(2) The Secretary of Health and Human Services shall first issue such final regulations (whether on an interim or other basis) before October 1, 1982, as may be necessary to implement the amendment made by subsection (a) on a timely basis. If such regulations are promulgated on an interim final basis, the Secretary shall take such steps as may be necessary to provide opportunity for public comment, and appropriate revision based thereon, so as to provide that such regulations are not on an interim basis later than January 31, 1983.

PAYMENTS TO HEALTH MAINTENANCE ORGANIZATIONS AND COMPETITIVE MEDICAL PLANS

SEC. 114. (a) Section 1876 of the Social Security Act is amended to read as follows:

"PAYMENTS TO HEALTH MAINTENANCE ORGANIZATIONS AND COMPETITIVE MEDICAL PLANS

"SEC. 1876. (a)(1)(A) The Secretary shall annually determine—

"(i) a per capita rate of payment for each class of individuals who are enrolled under this section with a eligible organization which has entered into a risk-sharing contract and who are entitled to benefits under part A and enrolled under part B, and

"(ii) a per capita rate of payment for each class of individuals who are so enrolled with such an organization and who are enrolled under part B only.

For purposes of this section, the term 'risk-sharing contract' means a contract entered into under subsection (g) and the term 'reasonable cost reimbursement contract' means a contract entered into under subsection (h).

"(B) The Secretary shall define appropriate classes of members, based on age, disability status, and such other factors as the Secretary determines to be appropriate, so as to ensure actuarial equivalence. The Secretary may add to, modify, or substitute for such classes, if such changes will improve the determination of actuarial equivalence.

"(C) The annual per capita rate of payment for each such class shall be equal to 95 percent of the adjusted average per capita cost (as defined in paragraph (4)) for that class.

"(D) In the case of a eligible organization with a risk-sharing contract, the Secretary shall make monthly payments in advance and in accordance with the rate determined under subparagraph (C) and except as provided in subsection (g)(2), to the organization for each individual enrolled with the organizaton under this section.

"(E) The amount of payment under this paragraph may be retroactively adjusted to take into account any difference between the actual number of individuals enrolled in the plan under this section and the number of such individuals estimated to be so enrolled in determining the amount of the advance payment.

"(2) With respect to any eligible organization which has entered into a reasonable cost reimbursement contract, payments shall be made to such plan in accordance with subsection (h)(2) rather than paragraph (1).

"(3) Payments under a contract to an eligible organization under paragraph (1) or (2) shall be instead of the amounts which (in the absence of the contract) would be otherwise payable, pursuant to sections 1814(b) and 1833(a), for services furnished by or through the organization to individuals enrolled with the organization under this section.

"(4) For purposes of this section, the term 'adjusted average per capita cost' means the average per capita amount that the Secretary estimates in advance (on the basis of actual experience, or retrospective actuarial equivalent based upon an adequate sample and other information and data, in a geographic area served by an eligible organization or in a similar area, with appropriate adjustments to assure actuarial equivalence) would be payable in any contract year for services covered under parts A and B, or part B only, and types of expenses otherwise reimbursable under parts A and B, or part B only (including administrative costs incurred by organizations described in sections 1816 and 1842), if the services were to be furnished by other than an eligible organization or, in the case of services covered only under section 1861(s)(2)(H), if the services were to be furnished by a physician or as an incident to a physician's service.

"(5) The payment to an eligible organization under this section for individuals enrolled under this section with the organization and entitled to benefits under part A and enrolled under part B shall be made from the Federal Hospital Insurance Trust Fund and the Federal Supplementary Medical Insurance Trust Fund. The portion of that payment to the organization for a month to be paid by the latter trust fund shall be equal to 200 percent of the sum of—

"(A) the product of (i) the number of such individuals for the month who have attained age 65, and (ii) the monthly actuarial

rate for supplementary medical insurance for the month as determined under section 1839(c)(1), and

"(B) the product of (i) the number of such individuals for the month who have not attained age 65, and (ii) the monthly actuarial rate for supplementary medical insurance for the month as determined under section 1839(c)(4).

The remainder of that payment shall be paid by the former trust fund.

"(6) If an individual is enrolled under this section with an eligible organization having a risk-sharing contract, only the eligible organization shall be entitled to receive payments from the Secretary under this title for services furnished to the individual.

"(b) For purposes of this section, the term 'eligible organization' means a public or private entity (which may be a health maintenance organization or a competitive medical plan), organized under the laws of any State, which—

"(1) is a qualified health maintenance organization (as defined in section 1310(d) of the Public Health Service Act), or

"(2) meets the following requirements:

"(A) The entity provides to enrolled members at least the following health care services:

"(i) Physicians' services performed by physicians (as defined in section 1861(r)(1)).

"(ii) Inpatient hospital services.

"(iii) Laboratory, X-ray, emergency, and preventive services.

"(iv) Out-of-area coverage.

"(B) The entity is compensated (except for deductibles, coinsurance, and copayments) for the provision of health care services to enrolled members by a payment which is paid on a periodic basis without regard to the date the health care services are provided and which is fixed without regard to the frequency, extent, or kind of health care service actually provided to a member.

"(C) The entity provides physicians' services primarily (i) directly through physicians who are either employees or partners of such organization, or (ii) through contracts with individual physicians or one or more groups of physicians (organized on a group practice or individual practice basis).

"(D) The entity assumes full financial risk on a prospective basis for the provision of the health care services listed in paragraph (1), except that such entity may—

"(i) obtain insurance or make other arrangements for the cost of providing to any enrolled member health care services listed in subparagraph (A) the aggregate value of which exceeds $5,000 in any year,

"(ii) obtain insurance or make other arrangements for the cost of health care service listed in subparagraph (A) provided to its enrolled members other than through the entity because medical necessity required their provision before they could be secured through the entity,

"(iii) obtain insurance or make other arrangements for not more than 90 percent of the amount by which

its costs for any of its fiscal years exceed 115 percent of its income for such fiscal year, and

"(iv) make arrangements with physicians or other health professionals, health care institutions, or any combination of such individuals or institutions to assume all or part of the financial risk on a prospective basis for the provision of basic health services by the physicians or other health professionals or through the institutions.

"(E) The entity has made adequate provision against the risk of insolvency, which provision is satisfactory to the Secretary.

Paragraph (2)(A)(ii) shall not apply to an entity which had contracted with a single State agency administering a State plan approved under title XIX for the provision of services (other than inpatient hospital services) to individuals eligible for such services under such State plan on a prepaid risk basis prior to 1970.

"(c)(1) The Secretary may not enter into a contract under this section with an eligible organization unless it meets the requirements of this subsection and subsection (e) with respect to members enrolled under this section.

"(2) The organization must provide to members enrolled under this section, through providers and other persons that meet the applicable requirements of this title and part A of title XI—

"(A) only those services covered under parts A and B of this title, for those members entitled to benefits under part A and enrolled under part B, or

"(B) only those services covered under part B, for those members enrolled only under such part,

which are available to individuals residing in the geographic area served by the organization, except that (i) the organization may provide such members with such additional health care services as the members may elect, at their option, to have covered, and (ii) in the case of an organization with a risk-sharing contract, the organization may provide such members with such additional health care services as the Secretary may approve. The Secretary shall approve any such additional health care services which the organization proposes to offer to such members, unless the Secretary determines that including such additional services will substantially discourage enrollment by covered individuals with the organization.

"(3)(A) Each eligible organization must have an open enrollment period, for the enrollment of individuals under this section, of at least 30 days duration every year, and must provide that at any time during which enrollments are accepted, the organization will accept up to the limits of its capacity (as determined by the Secretary) and without restrictions, except as may be authorized in regulations, individuals who are eligible to enroll under subsection (d) in the order in which they apply for enrollment, unless to do so would result in failure to meet the requirements of subsection (f) or would result in the enrollment of enrollees substantially nonrepresentative, as determined in accordance with regulations of the Secretary, of the population in the geographic area served by the organization.

"(B) An individual may enroll under this section with an eligible organization in such manner as may be prescribed in regulations and may terminate his enrollment with the eligible organization as of the beginning of the first calendar month following a full calendar month after the request is made for such termination (or, in the case of financial insolvency of the organization, as may be prescribed by regulations) or, in the case of such an organization with a reasonable cost reimbursement contract, as may be prescribed by regulations.

"(C) The Secretary may prescribe the procedures and conditions under which an eligible organization that has entered into a contract with the Secretary under this subsection may inform individuals eligible to enroll under this section with the organization about the organization, or may enroll such individuals with the organization.

"(D) The organization must provide assurances to the Secretary that it will not expel or refuse to re-enroll any such individual because of the individual's health status or requirements for health care services, and that it will notify each such individual of such fact at the time of the individual's enrollment.

"(4) The organization must—

"(A) make the services described in paragraph (2) (and such other health care services as such individuals have contracted for) (i) available and accessible to each such individual, within the area served by the organization, promptly as appropriate and in a manner which assures continuity, and (ii) when medically necessary, available and accessible twenty-four hours a day and seven days a week, and

"(B) provide for reimbursement with respect to services which are described in subparagraph (A) and which are provided to such an individual other than through the organization, if (i) the services were medically necessary and immediately required because of an unforeseen illness, injury, or condition and (ii) it was not reasonable given the circumstances to obtain the services through the organization.

"(5)(A) The organization must provide meaningful procedures for hearing and resolving grievances between the organization (including any entity or individual through which the organization provides health care services) and members enrolled with the organization under this section.

"(B) A member enrolled with an eligible organization under this section who is dissatisfied by reason of his failure to receive any health service to which he believes he is entitled and at no greater charge than he believes he is required to pay is entitled, if the amount in controversy is $100 or more, to a hearing before the Secretary to the same extent as is provided in section 205(b), and in any such hearing the Secretary shall make the eligible organization a party. If the amount in controversy is $1,000 or more, the individual or eligible organization shall, upon notifying the other party, be entitled to judicial review of the Secretary's final decision as provided in section 205(g), and both the individual and the eligible organization shall be entitled to be parties to that judicial review.

"(6) The organization must have arrangements, established in accordance with regulations of the Secretary, for an ongoing quality

assurance program for health care services it provides to such individuals, which program (A) stresses health outcomes and (B) provides review by physicians and other health care professionals of the process followed in the provision of such health care services.

"(d) Subject to the provisions of subsection (c)(3), every individual entitled to benefits under part A and enrolled under part B or enrolled under part B only (other than an individual medically determined to have end-stage renal disease) shall be eligible to enroll under this section with any eligible organization with which the Secretary has entered into a contract under this section and which serves the geographic area in which the individual resides.

"(e)(1) In no case may—

"(A) the portion of an eligible organization's premium rate and the actuarial value of its deductibles, coinsurance, and copayments charged (with respect to services covered under parts A and B) to individuals who are enrolled under this section with the organization and who are entitled to benefits under part A and enrolled under part B, or

"(B) the portion of its premium rate and the actuarial value of its deductibles, coinsurance, and copayments charged (with respect to services covered under part B) to individuals who are enrolled under this section with the organization and enrolled under part B only

exceed the actuarial value of the coinsurance and deductibles that would be applicable on the average to individuals enrolled under this section with the organization (or, if the Secretary finds that adequate data are not available to determine that actuarial value, the actuarial value of the coinsurance and deductibles applicable on the average to individuals in the area, in the State, or in the United States, eligible to enroll under this section with the organization, or other appropriate data) and entitled to benefits under part A and enrolled under part B, or enrolled under part B only, respectively, if they were not members of an eligible organization.

"(2) If the eligible organization provides to its members enrolled under this section services in addition to services covered under parts A and B of this title, election of coverage for such additional services (unless such services have been approved by the Secretary under subsection (c)(2)) shall be optional for such members and such organization shall furnish such members with information on the portion of its premium rate or other charges applicable to such additional services. In no case may the sum of—

"(A) the portion of such organization's premium rate charged, with respect to such additional services, to members enrolled under this section, and

"(B) the actuarial value of its deductibles, coinsurance, and copayments charged, with respect to such services to such members

exceed the adjusted community rate for such services.

"(3) For purposes of this section, the term 'adjusted community rate' for a service or services means, at the election of an eligible organization, either—

"(A) the rate of payment for that service or services which the Secretary annually determines would apply to a member enrolled under this section with an eligible organization if the

rate of payment were determined under a 'community rating system' (as defined in section 1302(8) of the Public Health Service Act, other than subparagraph (C)), or

"(B) such portion of the weighted aggregate premium, which the Secretary annually estimates would apply to a member enrolled under this section with the eligible organization, as the Secretary annually estimates is attributable to that service or services,

but adjusted for differences between the utilization characteristics of the members enrolled with the eligible organization under this section and the utilization characteristics of the other members of the organization (or, if the Secretary finds that adequate data are not available to adjust for those differences, the differences between the utilization characteristics of members in other eligible organizations, or individuals in the area, in the State, or in the United States, eligible to enroll under this section with an eligible organization and the utilization characteristics of the rest of the population in the area, in the State, or in the United States, respectively).

"(4) Notwithstanding any other provision of law, the eligible organization may (in the case of the provision of services to a member enrolled under this section for an illness or injury for which the member is entitled to benefits under a workmen's compensation law or plan of the United States or a State, under an automobile or liability insurance policy or plan, including a self-insured plan, or under no fault insurance) charge or authorize the provider of such services to charge, in accordance with the charges allowed under such law or policy—

"(A) the insurance carrier, employer, or other entity which under such law, plan, or policy is to pay for the provision of such services, or

"(B) such member to the extent that the member has been paid under such law, plan, or policy for such services.

"(f)(1) Each eligible organization with which the Secretary enters into a contract under this section shall have, for the duration of such contract, an enrolled membership at least one-half of which consists of individuals who are not entitled to benefits under this title or under a State plan approved under title XIX.

"(2) The Secretary may modify or waive the requirement imposed by paragraph (1) only if the Secretary determines that—

"(A) special circumstances warrant such modification or waiver, and

"(B) the eligible organization has taken and is making reasonable efforts to enroll individuals who are not entitled to benefits under this title or under a State plan approved under title XIX.

"(g)(1) The Secretary may enter a risk-sharing contract with any eligible organization, as defined in subsection (b)(1), which has at least 5,000 members, except that the Secretary may enter into such a contract with an eligible organization that has fewer members if the organization primarily serves members residing outside of urbanized areas.

"(2) Each risk-sharing contract shall provide that—

"(A) if the adjusted community rate, as defined in subsection (e)(3), for services under parts A and B (as reduced for the actu-

arial value of the coinsurance and deductibles under those parts) for members enrolled under this section with the organization and entitled to benefits under part A and enrolled in part B, or

"(B) if the adjusted community rate for services under part B (as reduced for the actuarial value of the coinsurance and deductibles under that part) for members enrolled under this section with the organization and entitled to benefits under part B only

is less than the average of the per capita rates of payment to be made under subsection (a)(1) at the beginning of an annual contract period for members enrolled under this section with the organization and entitled to benefits under part A and enrolled in part B, or enrolled in part B only, respectively, the eligible organization shall provide to members enrolled under a risk-sharing contract under this section with the organization and entitled to benefits under part A and enrolled in part B, or enrolled in part B only, respectively, the additional benefits described in paragraph (3) which are selected by the eligible organization and which the Secretary finds are at least equal in value to the difference between that average per capita payment and the adjusted community rate (as so reduced); except that this paragraph shall not apply with respect to any organization which elects to receive a lesser payment to the extent that there is no longer a difference between the average per capita payment and adjusted community rate (as so reduced). If the Secretary finds that there is insufficient enrollment experience to determine an average of the per capita rates of payment to be made under subsection (a)(1) at the beginning of a contract period, the Secretary may determine such an average based on the enrollment experience of other contracts entered into under this section.

"(3) The additional benefits referred to in paragraph (2) are—

"(A) the reduction of the premium rate or other charges made with respect to services furnished by the organization to members enrolled under this section, or

"(B) the provision of additional health benefits,

or both.

"(h)(1) If—

"(A) the Secretary is not satisfied that an eligible organization has the capacity to bear the risk of potential losses under a risk-sharing contract under this section, or

"(B) the eligible organization so elects or has an insufficient number of members to be eligible to enter into a risk-sharing contract under subsection (g)(1),

the Secretary may, if he is otherwise satisfied that the eligible organization is able to perform its contractual obligations effectively and efficiently, enter into a contract with such organization pursuant to which such organization is reimbursed on the basis of its reasonable cost (as defined in section 1861(v)) in the manner prescribed in paragraph (3).

"(2) A reasonable cost reimbursement contract under this subsection may, at the option of such organization, provide that the Secretary—

"(A) will reimburse hospitals and skilled nursing facilities either for the reasonable cost (as determined under section

1861(v)) or for payment amounts determined in accordance with section 1886, as applicable, of services furnished to individuals enrolled with such organization pursuant to subsection (d), and

"(B) will deduct the amount of such reimbursement from payment which would otherwise be made to such organization.

If such an eligible organization pays a hospital or skilled nursing facility directly, the amount paid shall not exceed the reasonable cost of the services (as determined under section 1861(v)) or the amount determined under section 1886, as applicable, unless such organization demonstrates to the satisfaction of the Secretary that such excess payments are justified on the basis of advantages gained by the organization.

"(3) Payments made to an organization with a reasonable cost reimbursement contract shall be subject to appropriate retroactive corrective adjustment at the end of each contract year so as to assure that such organization is paid for the reasonable cost actually incurred (excluding any part of incurred cost found to be unnecessary in the efficient delivery of health services) or the amounts otherwise determined under section 1886 for the types of expenses otherwise reimbursable under this title for providing services covered under this title to individuals described in subsection (a)(1).

"(4) Any reasonable cost reimbursement contract with an eligible organization under this subsection shall provide that the Secretary shall require, at such time following the expiration of each accounting period of the eligible organization (and in such form and in such detail) as he may prescribe—

"(A) that the organization report to him in an independently certified financial statement its per capita incurred cost based on the types of components of expenses otherwise reimbursable under this title for providing services described in subsection (a)(1), including therein, in accordance with accounting procedures prescribed by the Secretary, its methods of allocating costs between individuals enrolled under this section and other individuals enrolled with such organization;

"(B) that failure to report such information as may be required may be deemed to constitute evidence of likely overpayment on the basis of which appropriate collection action may be taken;

"(C) that in any case in which an eligible organization is related to another organization by common ownership or control, a consolidated financial statement shall be filed and that the allowable costs for such organization may not include costs for the types of expense otherwise reimbursable under this title, in excess of those which would be determined to be reasonable in accordance with regulations (providing for limiting reimbursement to costs rather than charges to the eligible organization by related organizations and owners) issued by the Secretary; and

"(D) that in any case in which compensation is paid by an eligible organization substantially in excess of what is normally paid for similar services by similar practitioners (regardless of method of compensation), such compensation may as appropriate be considered to constitute a distribution of profits.

"(i)(1) Each contract under this section shall be for a term of at least one year, as determined by the Secretary, and may be made

automatically renewable from term to term in the absence of notice by either party of intention to terminate at the end of the current term; except that the Secretary may terminate any such contract at any time (after such reasonable notice and opportunity for hearing to the eligible organization involved as he may provide in regulations), if he finds that the organization—

"(A) has failed substantially to carry out the contract,

"(B) is carrying out the contract in a manner inconsistent with the efficient and effective administration of this section, or

"(C) no longer substantially meets the applicable conditions of subsections (b), (c), and (e).

"(2) The effective date of any contract executed pursuant to this section shall be specified in the contract.

"(3) Each contract under this section—

"(A) shall provide that the Secretary, or any person or organization designated by him—

"(i) shall have the right to inspect or otherwise evaluate (I) the quality, appropriateness, and timeliness of services performed under the contract and (II) the facilities of the organization when there is reasonable evidence of some need for such inspection, and

"(ii) shall have the right to audit and inspect any books and records of the eligible organization that pertain (I) to the ability of the organization to bear the risk of potential financial losses, or (II) to services performed or determinations of amounts payable under the contract;

"(B) shall require the organization with a risk-sharing contract to provide (and pay for) written notice in advance of the contract's termination, as well as a description of alternatives for obtaining benefits under this title, to each individual enrolled under this section with the organization; and

"(C) shall require the organization to comply with subsections (a) and (c) of section 1318 of the Public Health Service Act (relating to disclosure of certain financial information) and with the requirement of section 1301(c)(8) of such Act (relating to liability arrangements to protect members); and

"(D) shall contain such other terms and conditions not inconsistent with this section (including requiring the organization to provide the Secretary with such information) as the Secretary may find necessary and appropriate.

"(4) The Secretary may not enter into a risk-sharing contract with an eligible organization if a previous risk-sharing contract with that organization under this section was terminated at the request of the organization within the preceding five-year period, except in circumstances which warrant special consideration, as determined by the Secretary.

"(5) The authority vested in the Secretary by this section may be performed without regard to such provisions of law or regulations relating to the making, performance, amendment, or modification of contracts of the United States as the Secretary may determine to be inconsistent with the furtherance of the purpose of this title.".

(b) Section 1861(s)(2) of the Social Security Act is amended—

(1) by striking out "and" at the end of subparagraph (F);

(2) by inserting "and" after the semicolon in subparagraph (G); and

(3) by adding after subparagraph (G) the following new subparagraph:

"(H) services furnished pursuant to a contract under section 1876 to a member of an eligible organization by a physician assistant or by a nurse practitioner (as defined in subsection (aa)(3)) and such services and supplies furnished as an incident to his service to such a member as would otherwise be covered under this part if furnished by a physician or as an incident to a physician's service;".

(c)(1) Subject to paragraph (2), the amendment made by subsection (a) shall apply with respect to services furnished on or after the initial effective date (as defined in paragraph (4)), except that such amendment shall not apply—

(A) with respect to services furnished by an eligible organization to any individual who is enrolled with that organization under an existing cost contract (as defined in paragraph (3)(A)) and entitled to benefits under part A, or enrolled in part B, of title XVIII of the Social Security Act at the time the organization first enters into a new risk-sharing contract (as defined in paragraph (3)(D)) unless—

(i) the individual requests at any time that the amendment apply, or

(ii) the Secretary determines at any time that the amendment should apply to all members of the organization because of administrative costs or other administrative burdens involved and so informs in advance each affected member of the eligible organization;

(B) with respect to services furnished by an eligible organization during the five-year period beginning on the initial effective date, if—

(i) the organization has an existing risk-sharing contract (as defined in paragraph (3)(B)) on the initial effective date, or

(ii) on the date of the enactment of this Act the organization was furnishing services pursuant to an existing demonstration project (as defined in paragraph (3)(C)), such demonstration project is concluded before the initial effective date, and before such initial effective date the organization enters into an existing risk-sharing contract,

unless the organization requests that the amendment apply earlier; or

(C) with respect to services furnished by an eligible organization during the period of an existing demonstration project if on the initial effective date the organization was furnishing services pursuant to the project and if the project concludes after such date.

(2)(A) In the case of an eligible organization which has in effect an existing cost contract (as defined in paragraph (3)(A)) on the initial effective date, the organization may receive payment under a new risk-sharing contract with respect to a current, nonrisk medicare enrollee (as defined in subparagraph (C)) only to the extent that the organization enrolls, for each such enrollee, two new medicare

enrollees (as defined in subparagraph (D)). The selection of those current nonrisk medicare enrollees with respect to whom payment may be so received under a new risk-sharing contract shall be made in a nonbiased manner.

(B) Subparagraph (A) shall not be construed to prevent an eligible organization from providing for enrollment, on a basis described in subsection (a)(6) of section 1876 of the Social Security Act (as amended by this Act, other than under a reasonable cost reimbursement contract), of current, nonrisk medicare enrollees and from providing such enrollees with some or all of the additional benefits described in section 1876(g)(2) of the Social Security Act (as amended by this Act), but (except as provided in subparagraph (A))—

(i) payment to the organization with respect to such enrollees shall only be made in accordance with the terms of a reasonable cost reimbursement contract, and

(ii) no payment may be made under section 1876 of such Act with respect to such enrollees for any such additional benefits.

Individuals enrolled with the organization under this subparagraph shall be considered to be individuals enrolled with the organization for the purpose of meeting the requirement of section 1876(g)(2) of the Social Security Act (as amended by this Act).

(C) For purposes of this paragraph, the term "current, nonrisk medicare enrollee" means, with respect to an organization, an individual who on the initial effective date—

(i) is enrolled with that organization under an existing cost contract, and

(ii) is entitled to benefits under part A, or enrolled in part B, of title XVIII of the Social Security Act.

(D) For purposes of this paragraph, the term "new medicare enrollee" means, with respect to an organization, an individual who—

(i) is enrolled with the organization after the date the organization first enters into a new risk-sharing contract,

(ii) at the time of such enrollment is entitled to benefits under part A, or enrolled in part B, of title XVIII of the Social Security Act, and

(iii) was not enrolled with the organization at the time the individual became entitled to benefits under part A, or to enroll in part B, of such title.

(3) For purposes of this subsection:

(A) The term "existing cost contract" means a contract which is entered into under section 1876 of the Social Security Act, as in effect before the initial effective date, or reimbursement on a reasonable cost basis under section 1833(a)(1)(A) of such Act, and which is not an existing risk-sharing contract or an existing demonstration project.

(B) The term "existing risk-sharing contract" means a contract entered into under section 1876(i)(2)(A) of the Social Security Act, as in effect before the initial effective date.

(C) The term "existing demonstration project" means a demonstration project under section 402(a) of the Social Security Amendments of 1967 or under section 222(a) of the Social Security Amendments of 1972, relating to the provision of services for which payment may be made under title XVIII of the Social Security Act.

(D) The term "new risk-sharing contract" means a contract entered into under section 1876(g) of the Social Security Act, as amended by this Act.

(E) The term "reasonable cost reimbursement contract" means a contract entered into under section 1833(a)(1) of the Social Security Act or under section 1876(h) of such Act, as amended by this Act.

(4) As used in this section, the term "initial effective date" means—

(A) the first day of the thirteenth month which begins after the date of the enactment of this Act, or

(B) the first day of the first month after the month in which the Secretary of Health and Human Services notifies the Committee on Finance of the Senate and the Committees on Ways and Means and on Energy and Commerce of the House of Representatives that he is reasonably certain that the methodology to make appropriate adjustments (referred to in section 1876(a)(4) of the Social Security Act, as amended by this Act) has been developed and can be implemented to assure actuarial equivalence in the estimation of adjusted average per capita costs under that section,

whichever is later.

(d) The Secretary of Health and Human Services shall conduct a study of the additional benefits selected by eligible organizations pursuant to section 1876(g)(2) of the Social Security Act, as amended by subsection (a) of this section. The Secretary shall report to the Congress within 24 months of the initial effective date (as defined in subsection (c)(4)) with respect to the findings and conclusions made as a result of such study.

(e) The Secretary of Health and Human Services shall conduct a study evaluating the extent of, and reasons for, the termination by medicare beneficiaries of their memberships in organizations with contracts under section 1876 of the Social Security Act. Such study may be coordinated with the study provided for under section 2178(d) of the Omnibus Budget Reconciliation Act of 1981. In conducting such study, the Secretary shall place special emphasis on the quantity and quality of medical care provided in such organizations and the quality of such care when provided on a fee-for-service basis. The Secretary shall submit an interim report to the Congress, within two years after the initial effective date (as defined in subsection (c)(4)), and a final report within five years after such date containing the respective interim and final findings and conclusions made as a result of such study.

PROHIBITION OF PAYMENT FOR INEFFECTIVE DRUGS

SEC. 115. (a) Effective September 30, 1982, section 131 of Public Law 97-92 is repealed, and the provisions of such section, and of section 210 of the Departments of Labor, Health and Human Services, and Education and Related Agencies Appropriation Act, 1982 (H.R. 4560), as passed by the House of Representatives on October 6, 1981, and of section 209 of such Act as reported by the Senate Committee on Appropriations on November 9, 1981, shall not apply to *any sums appropriated for fiscal year 1983 or any succeeding fiscal year.*

(b) No provision of law limiting the use of funds for purposes of enforcing or implementing section 1862(c) or section 1903(i)(5) of the Social Security Act, section 2103 of the Omnibus Budget Reconciliation Act of 1981, or any rule or regulation issued pursuant to any such section (including any provision contained in, or incorporated by reference into, any appropriation Act or resolution making continuing appropriations) shall apply to any period after September 30, 1982, unless such provision of law is enacted after the date of the enactment of this Act and specifically states that such provision is to supersede this section.

MEDICARE PAYMENTS SECONDARY FOR OLDER WORKERS COVERED UNDER GROUP HEALTH PLANS

SEC. 116. (a) Section 4 of the Age Discrimination in Employment Act of 1967 is amended by adding at the end thereof the following new subsection:

"(g)(1) For purposes of this section, any employer must provide that any employee aged 65 through 69 shall be entitled to coverage under any group health plan offered to such employees under the same conditions as any employee under age 65.

"(2) For purposes of paragraph (1), the term 'group health plan' has the meaning given to such term in section 162(i)(2) of the Internal Revenue Code of 1954.".

(b) Section 1862(b) of the Social Security Act is amended by adding at the end thereof the following new paragraph:

"(3)(A)(i) Payment under this title may not be made, except as provided in clause (ii), with respect to any item or service furnished during the period described in clause (iii) to an individual who is over 64 but under 70 years of age (or to the spouse of such individual, if the spouse is over 64 but under 70 years of age) who is employed at the time such item or service is furnished to the extent that payment with respect to expenses for such item or service has been made, or can reasonably be expected to be made, under a group health plan (as defined in clause (iv)) under which such individual is covered by reason of such employment.

"(ii) Any payment under this title with respect to any item or service during the period described in clause (iii) shall be conditioned on reimbursement to the appropriate Trust Fund established by this title when notice or other information is received that payment for such item or service has been made under a group health plan. The Secretary may waive the provisions of this clause in the case of an individual claim if he determines that the probability of recovery or amount involved in such claim does not warrant the pursuing of the claim.

"(iii) The provisions of clauses (i) and (ii) shall apply to an individual only for the period beginning with the month in which such individual becomes entitled to benefits under this title under section 226(a) and ending with the month in which such individual attains the age of 70 and shall not include any month for which the individual would, upon application, be entitled to benefits under section 226A.

"(iv) For purposes of this paragraph, the term 'group health plan' has the meaning given to such term in section 162(i)(2) of the Internal Revenue Code of 1954.

"(B) Where payment for an item or service under a group health plan is less than the amount of the charge for such item or service, payment may be made under this title (without regard to deductibles and coinsurance under this title) for the remainder of such charge, but—

"(i) such payment under this title may not exceed an amount which would be payable under this title for such item or service in the absence of such group health plan; and

"(ii) such payment under this title, when combined with the amount payable under such plan, may not exceed—

"(I) in the case of an item or service payment for which is determined under this title on the basis of reasonable cost (or other cost-related basis) or under section 1886, the amount which would be payable under this title on such basis; and

"(II) in the case of an item or service for which payment is authorized under this title on another basis, the greater of—

"(a) the amount which would be payable under the group health plan (without regard to deductibles and coinsurance under such plan), or

"(b) the reasonable charge or other amount which would be payable under this title (without regard to deductibles and coinsurance under this title).".

(c) The amendment made by subsection (a) shall become effective on January 1, 1983, and the amendment made by subsection (b) shall apply with respect to items and services furnished on or after such date.

INTEREST CHARGES ON OVERPAYMENTS AND UNDERPAYMENTS

SEC. 117. (a)(1) Section 1815 of the Social Security Act is amended by adding at the end the following new subsection:

"(d) Whenever a final determination is made that the amount of payment made under this part to a provider of services was in excess of or less than the amount of payment that is due, and payment of such excess or deficit is not made (or effected by offset) within 30 days of the date of the determination, interest shall accrue on the balance of such excess or deficit not paid or offset (to the extent that the balance is owed by or owing to the provider) at a rate determined in accordance with the regulations of the Secretary of the Treasury applicable to charges for late payments.".

(2) Section 1833 of such Act is amended by adding at the end the following new subsection:

"(j) Whenever a final determination is made that the amount of payment made under this part either to a provider of services or to another person pursuant to an assignment under section 1842(b)(3)(B)(ii) was in excess of or less than the amount of payment that is due, and payment of such excess or deficit is not made (or effected by offset) within 30 days of the date of the determination, interest shall accrue on the balance of such excess or deficit not

paid or offset (to the extent that the balance is owed by or owing to the provider) at a rate determined in accordance with the regulations of the Secretary of the Treasury applicable to charges for late payments.".

(b) The amendments made by subsection (a) apply to final determinations made on or after the date of the enactment of this Act.

AUDIT AND MEDICAL CLAIMS REVIEW

SEC. 118. In addition to any funds otherwise provided for fiscal years 1983, 1984, and 1985 for payments to intermediaries and carriers under agreements entered into under sections 1816 and 1842 of the Social Security Act, there are transferred from the Federal Hospital Insurance Trust Fund and the Federal Supplementary Medical Insurance Fund in such proportions as the Secretary of Health and Human Services determines to be appropriate, an additional $45,000,000 for each of such fiscal years for payments to such intermediaries and carriers under such agreements to be used exclusively for the purpose of carrying out provider cost audits and reviews of medical necessity, consistent with the provisions of sections 1816 and 1842 of the Social Security Act.

PRIVATE SECTOR REVIEW INITIATIVE

SEC. 119. (a) The Secretary of Health and Human Services shall undertake an initiative to improve medical review by intermediaries and carriers under title XVIII of Social Security Act and to encourage similar review efforts by private insurers and other private entities. The initiative shall include the development of specific standards for measuring the performance of such intermediaries and carriers with respect to the identification and reduction of unnecessary utilization of health services.

(b) Where such review activity results in the denial of payment to providers of services under title XVIII of the Social Security Act, such providers shall be prohibited, in accordance with sections 1866 and 1879 of such title, from collecting any payments from beneficiaries unless otherwise provided under such title.

TEMPORARY DELAY IN PERIODIC INTERIM PAYMENTS

SEC. 120. Notwithstanding section 1815(a) of the Social Security Act, in the case of a hospital which is paid periodic interim payments under such section, the Secretary of Health and Human Services shall provide that—

(1) with respect to the last 21 days for which such payments would otherwise be made during fiscal year 1983, such payments shall be deferred until fiscal year 1984; and

(2) with respect to the last 21 days for which such payments would otherwise be made during fiscal year 1984, such payments shall be deferred until fiscal year 1985.

(B) Section 1814 of such Act is further amended by adding at the end the following new subsection:

"Payment for Hospice Care

"(i)(1) Subject to the limitation under paragraph (2) and the provisions of section 1813(a)(4), the amount paid to a hospice program with respect to hospice care for which payment may be made under this part shall be an amount equal to the costs which are reasonable and related to the cost of providing hospice care or which are based on such other tests of reasonableness as the Secretary may prescribe in regulations (including those authorized under section 1861(v)(1)(A)), except that no payment may be for bereavement counseling and no reimbursement may be made for other counseling services (including nutritional and dietary counseling) as separate services.

"(2)(A) The amount of payment made under this part for hospice care provided by (or under arrangements made by) a hospice program located in a region (as defined by the Secretary) for an accounting year may not exceed the 'cap amount' for the region for the year (computed under subparagraph (B)) multiplied by the number of medicare beneficiaries in the hospice program in that year (determined under subparagraph (C)).

"(B) For purposes of subparagraph (A), the 'cap amount' for a region for a year is computed as follows:

"(i) The Secretary, using records of the program under this title, shall identify individuals (or a representative sample of such individuals)—

"(I) who died during the base period (as defined in clause (v)),

"(II) with respect to whom the primary cause of death was cancer, and

"(III) who, during the six-month period preceding death, were provided benefits under this title.

"(ii) The Secretary shall determine a national average medicare per capita expenditure amount by (I) determining (or estimating) the amount of payments made under this title with respect to services provided to individuals identified in clause (i) during the six months before death, and (II) dividing such amount of payments by the number of such individuals.

"(iii) The Secretary, using the best available data, shall then compute a regional average medicare per capita expenditure amount for each region, by adjusting the national average medicare per capita expenditure amount (computed under clause (ii)) to reflect the relative difference between that region's average cost of delivering health care and the national average cost of delivering health care.

"(iv) The 'cap amount' for a region for an accounting year is 40 percent of the regional average determined under clause (iii) for that region, increased or decreased by the same percentage as the percentage increase or decrease, respectively, in the medical care expenditure category of the consumer price index for all urban consumers (U.S. city average), published by the Bureau of

Labor Statistics, from the fourth month of the base period to the fifth month of the accounting year.

"(v) For purposes of this subparagraph, the term 'base period' means the most recent period of 12 months (ending before the date proposed regulations are first issued to carry out this paragraph) for which the Secretary determines he has sufficient data to make the determinations required under clauses (i) through (iii).

"(C) For purposes of subparagraph (A), the 'number of medicare beneficiaries' in a hospice program in an accounting year is equal to the number of individuals who have made an election under subsection (d) with respect to the hospice program and have been provided hospice care by (or under arrangements made by) the hospice program under this part in the accounting year, such number reduced to reflect the proportion of hospice care that each such individual was provided in a previous or subsequent accounting year or under a plan of care established by another hospice program.".

(3) Section 1816(e) of such Act is amended by adding at the end thereof the following new paragraph:

"(5) Notwithstanding any other provision of this title, the Secretary shall designate the agency or organization which has entered into an agreement under this section to perform functions under such an agreement with respect to each hospice program, except that with respect to a hospice program which is a subdivision of a provider of services (and such hospice program and provider of services are under common control) due regard shall be given to the agency or organization which performs the functions under this section for the provider of services.".

(d)(1) Section 1861(u) of the Social Security Act is amended by inserting "hospice program," after "home health agency,".

(2) Section 1861(w)(1) of such Act is amended by striking out "or home health agency" and by inserting in lieu thereof "home health agency, or hospice program".

(3) Section 1861 of such Act is further amended by adding at the end the following new subsection:

"Hospice Care; Hospice Program

"(dd)(1) The term 'hospice care' means the following items and services provided to a terminally ill individual by, or by others under arrangements made by, a hospice program under a written plan (for providing such care to such individual) established and periodically reviewed by the individual's attending physician and by the medical director (and by the interdisciplinary group described in paragraph (2)(B)) of the program—

"(A) nursing care provided by or under the supervision of a registered professional nurse,

"(B) physical or occupational therapy or speech-language pathology,

"(C) medical social services under the direction of a physician,

"(D)(i) services of a home health aide who has successfully completed a training program approved by the Secretary and (ii) homemaker services,

PART II—CHANGES IN BENEFITS, PREMIUMS, AND ENROLLMENT

MEDICARE COVERAGE OF FEDERAL EMPLOYEES

SEC. 121. For provisions providing certain employees of the United States and instrumentalities thereof with entitlement to hospital insurance benefits under part A of title XVIII of the Social Security Act, see section 278 of this Act.

HOSPICE CARE

SEC. 122. (a)(1) Section 1811 of the Social Security Act is amended by striking out "and home health services" and inserting in lieu thereof "home health services, and hospice care".

(2) Section 7(d)(1) of the Railroad Retirement Act of 1974 is amended by inserting "hospice care," after "home health services,".

(b)(1) Section 1812(a) of the Social Security Act is amended by striking out "and" at the end of paragraph (2), by striking out the period at the end of paragraph (3) and inserting in lieu thereof "; and", and by adding after paragraph (3) the following new paragraph:

> *"(4) in lieu of certain other benefits, hospice care with respect to the individual during up to two periods of 90 days each and one subsequent period of 30 days with respect to which the individual makes an election under subsection (d)(1).".*

(2) Section 1812 of such Act is further amended by inserting after subsection (c) the following new subsection:

"(d)(1) Payment under this part may be made for hospice care provided with respect to an individual only during two periods of 90 days each and one subsequent period of 30 days during the individual's lifetime and only, with respect to each such period, if the individual makes an election under this paragraph to receive hospice care under this part provided by, or under arrangements made by, a particular hospice program instead of certain other benefits under this title.

"(2)(A) Except as provided in subparagraphs (B) and (C) and except in such exceptional and unusual circumstances as the Secretary may provide, if an individual makes such an election for a period with respect to a particular hospice program, the individual shall be deemed to have waived all rights to have payment made under this title with respect to—

> *"(i) hospice care provided by another hospice program (other than under arrangements made by the particular hospice program) during the period, and*
>
> *"(ii) services furnished during the period that are determined (in accordance with guidelines of the Secretary) to be—*
>
> > *"(I) related to the treatment of the individual's condition with respect to which a diagnosis of terminal illness has been made or*
> >
> > *"(II) equivalent to (or duplicative of) hospice care;*

except that clause (ii) shall not apply to physicians' services furnished by the individual's attending physician (if not an employee of the hospice program) or to other than services provided by (or under arrangements made by) the hospice program.

"(B) After an individual makes such an election with respect to a 90- or 30-day period, the individual may revoke the election during the period, in which case—

"(i) the revocation shall act as a waiver of the right to have payment made under this part for any hospice care benefits for the remaining time in such period and (for purposes of subsection (a)(4) and subparagraph (A)) the individual shall be deemed to have been provided such benefits during such entire period, and

"(ii) the individual may at any time after the revocation execute a new election for a subsequent period, if the individual otherwise is entitled to hospice care benefits with respect to such a period.

"(C) An individual may, once in each such period, change the hospice program with respect to which the election is made and such change shall not be considered a revocation of an election under subparagraph (B).

"(D) For purposes of this title, an individual's election with respect to a hospice program shall no longer be considered to be in effect with respect to that hospice program after the date the individual's revocation or change of election with respect to that election takes effect.".

(c)(1) Section 1814(a) of the Social Security Act is amended by striking out "and" at the end of paragraph (6), by striking out the period at the end of paragraph (7) and inserting in lieu thereof "; and", and by inserting after paragraph (7) the following new paragraph:

"(8) in the case of hospice care provided an individual—

"(A)(i) in the first 90-day period—

"(I) the individual's attending physician (as defined in section 1861(dd)(3)(B)), and

"(II) the medical director (or physician member of the interdisciplinary group described in section 1861(dd)(2)(B)) of the hospice program providing (or arranging for) the care,

each certify, not later than two days after hospice care is initiated, that the individual is terminally ill (as defined in section 1861(dd)(3)(A)), and

"(ii) in a subsequent 90- or 30-day period, the medical director or physician described in clause (i)(II) recertifies at the beginning of the period that the individual is terminally ill;

"(B) a written plan for providing hospice care with respect to such individual has been established (before such care is provided by, or under arrangements made by, that hospice program) and is periodically reviewed by the individual's attending physician and by the medical director (and the interdisciplinary group described in section 1861(dd)(2)(B)) of the hospice program; and

"(C) such care is being or was provided pursuant to such plan of care.".

(2)(A) Section 1814(b) of such Act is amended by inserting "(other than a hospice program providing hospice care)" after "The amount paid to any provider of services".

"(E) medical supplies (including drugs and biologicals) and the use of medical appliances, while under such a plan,

"(F) physicians' services,

"(G) short-term inpatient care (including both respite care and procedures necessary for pain control and acute and chronic symptom management) in an inpatient facility meeting such conditions as the Secretary determines to be appropriate to provide such care, but such respite care may be provided only on an intermittent, nonroutine, and occasional basis and may not be provided consecutively over longer than five days, and

"(H) counseling (including dietary counseling) with respect to care of the terminally ill individual and adjustment to his death.

The care and services described in subparagraphs (A) and (D) may be provided on a 24-hour, continuous basis only during periods of crisis (meeting criteria established by the Secretary) and only as necessary to maintain the terminally ill individual at home.

"(2) The term 'hospice program' means a public agency or private organization (or a subdivision thereof) which—

"(A)(i) is primarily engaged in providing the care and services described in paragraph (1) and makes such services available (as needed) on a 24-hour basis and which also provides bereavement counseling for the immediate family of terminally ill individuals,

"(ii) provides for such care and services in individuals' homes, on an outpatient basis, and on a short-term inpatient basis, directly or under arrangements made by the agency or organization, except that—

"(I) the agency or organization must routinely provide directly substantially all of each of the services described in subparagraphs (A), (C), (F), and (H) of paragraph (1), and

"(II) in the case of other services described in paragraph (1) which are not provided directly by the agency or organization, the agency or organization must maintain professional management responsibility for all such services furnished to an individual, regardless of the location or facility in which such services are furnished; and

"(iii) provides assurances satisfactory to the Secretary that the aggregate number of days of inpatient care described in paragraph (1)(G) provided in any 12-month period to individuals who have an election in effect under section 1812(d) with respect to that agency or organization does not exceed 20 percent of the aggregate number of days during that period on which such elections for such individuals are in effect;

"(B) has an interdisciplinary group of personnel which—

"(i) includes at least—

"(I) one physician (as defined in subsection (r)(1)),

"(II) one registered professional nurse, and

"(III) one social worker,

employed by the agency or organization, and also includes at least one pastoral or other counselor,

"(ii) provides (or supervises the provision of) the care and services described in paragraph (1), and

"(iii) establishes the policies governing the provision of such care and services;

"(C) maintains central clinical records on all patients;

"(D) does not discontinue the hospice care it provides with respect to a patient because of the inability of the patient to pay for such care;

"(E)(i) utilizes volunteers in its provision of care and services in accordance with standards set by the Secretary, which standards shall ensure a continuing level of effort to utilize such volunteers, and (ii) maintains records on the use of these volunteers and the cost savings and expansion of care and services achieved through the use of these volunteers;

"(F) in the case of an agency or organization in any State in which State or applicable local law provides for the licensing of agencies or organizations of this nature, is licensed pursuant to such law; and

"(G) meets such other requirements as the Secretary may find necessary in the interest of the health and safety of the individuals who are provided care and services by such agency or organization.

"(3)(A) An individual is considered to be 'terminally ill' if the individual has a medical prognosis that the individual's life expectancy is 6 months or less.

"(B) The term 'attending physician' means, with respect to an individual, the physician (as defined in subsection (r)(1)), who may be employed by a hospice program, whom the individual identifies as having the most significant role in the determination and delivery of medical care to the individual at the time the individual makes an election to receive hospice care.

"(4)(A) An entity which is certified as a provider of services other than a hospice program shall be considered, for purposes of certification as a hospice program, to have met any requirements under paragraph (2) which are also the same requirements for certification as such other type of provider. The Secretary shall coordinate surveys for determining certification under this title so as to provide, to the extent feasible, for simultaneous surveys of an entity which seeks to be certified as a hospice program and as a provider of services of another type.

"(B) Any entity which is certified as a hospice program and as a provider of another type shall have separate provider agreements under section 1866 and shall file separate cost reports with respect to costs incurred in providing hospice care and in providing other services and items under this title.".

(e) Section 1813(a) of such Act is amended by adding at the end the following new paragraph:

"(4)(A) The amount payable for hospice care shall be reduced—

"(i) in the case of drugs and biologicals provided on an outpatient basis by (or under arrangements made by) the hospice program, by a coinsurance amount equal to an amount (not to exceed $5 per prescription) determined in accordance with a drug copayment schedule (established by the hospice program) which is related to, and approximates 5 percent of, the cost of the drug or biological to the program, and

"(ii) in the case of respite care provided by (or under arrangements made by) the hospice program, by a coinsurance amount equal to 5 percent of the amount estimated by the hospice program (in accordance with regulations of the Secretary) to be equal to the amount of payment under section 1814(i) to that program for respite care;

except that the total of the coinsurance required under clause (ii) for an individual may not exceed for a hospice coinsurance period the inpatient hospital deductible applicable for the year in which the period began. For purposes of this subparagraph, the term 'hospice coinsurance period' means, for an individual, a period of consecutive days beginning with the first day for which an election under section 1812(d) is in effect for the individual and ending with the close of the first period of 14 consecutive days on each of which such an election is not in effect for the individual.

"(B) During the period of an election by an individual under section 1812(d)(1), no copayments or deductibles other than those under subparagraph (A) shall apply with respect to services furnished to such individual which constitute hospice care, regardless of the setting in which such services are furnished.".

(f) Section 1862(a) of the Social Security Act is amended—

(1) by amending paragraph (1) to read as follows:

"(1)(A) which, except for items and services described in subparagraph (B) or (C), are not reasonable and necessary for the diagnosis or treatment of illness or injury or to improve the functioning of a malformed body member,

"(B) in the case of items and services described in section 1861(s)(10), which are not reasonable and necessary for the prevention of illness, and

"(C) in the case of hospice care, which are not reasonable and necessary for the palliation or management of terminal illness;";

(2) by inserting "(except, in the case of hospice care, as is otherwise permitted under paragraph (1)(C))" in paragraph (6) after "comfort items";

(3) by striking out "paragraph (1)" in paragraph (7) and inserting in lieu thereof "paragraph (1)(B)"; and

(4) by inserting "(except, in the case of hospice care, as is otherwise permitted under paragraph (1)(C))" in paragraph (9) after "custodial care".

(g)(1) Section 1862(f) of the Social Security Act is amended by striking out "paragraph (1)" and inserting in lieu thereof "paragraph (1)(A)".

(2) Section 1863 of the Social Security Act is amended by striking out "and (cc)(2)(I)" and inserting in lieu thereof "(cc)(2)(I), and (dd)(2)".

(3) Section 1864(a) of such Act is amended—

(A) by inserting "or whether an agency is a hospice program" in the first sentence after "home health agency,"; and

(B) by striking out "or home health agency" in the second sentence and inserting in lieu thereof "home health agency, or hospice program".

(4) Section 1865(a) of such Act is amended by striking out "or (o)" in the last sentence and inserting in lieu thereof "(o), or (dd)".

(5) Section 1866(b)(2)(A) of such Act is amended by striking out "or (a)(3)" and inserting in lieu thereof "(a)(3), or (a)(4)".

(6) Section 1866(b)(4)(A) of such Act is amended by inserting "or hospice care" after "home health services".

(h)(1)(A) Subject to subparagraph (B), the amendments made by this section apply to hospice care provided on or after November 1, 1983, and before October 1, 1986.

(B) An individual who on October 1, 1986, has an election under section 1812(d)(1) of the Social Security Act in effect for a period, is entitled to hospice care benefits after that date during the remainder of that period and any consecutive period to which the individual would have been entitled before such date.

(2) In order to provide for the timely implementation of the amendments made by this Act, the Secretary of Health and Human Services shall, not later than September 1, 1983, promulgate such final regulations as may be necessary to set forth—

(A) a description of the care included in "hospice care" and the standards for qualification of a "hospice program", under section 1861(dd) of the Social Security Act, and

(B) the standards for payment for hospice care under part A of title XVIII of such Act, pursuant to section 1814(i) of such Act.

(h)(1) Notwithstanding any provision of law which has the effect of restricting the time period of a hospice demonstration project in effect on July 15, 1982, pursuant to section 402(a) of the Social Security Amendments of 1967, the Secretary of Health and Human Services, upon request of the hospice involved, shall permit continuation of the project until November 1, 1983, or, if later, the date on which payments can first be made to any hospice program under the amendments made by this section.

(2) Prior to September 30, 1983, the Secretary shall submit to Congress a report on the effectiveness of demonstration projects referred to in paragraph (1), including an evaluation of the cost-effectiveness of hospice care, the reasonableness of the 40 percent cap amount for hospice care as provided in section 1814(i) of the Social Security Act (as added by this section), proposed methodology for determining such cap amount, proposed standards for requiring and measuring the maintenance of effort for utilizing volunteers as required under section 1861(dd) of such Act, an evaluation of physician reimbursement for services furnished as a part of hospice care and for services furnished to individuals receiving hospice care but which are not reimbursed as a part of the hospice care, and any proposed legislative changes in the hospice care provisions of title XVIII of such Act.

(i)(1) The Secretary of Health and Human Services shall conduct a study and, prior to January 1, 1986, report to the Congress on whether or not the reimbursement method and benefit structure (including copayments) for hospice care under title XVIII of the Social Security Act are fair and equitable and promote the most efficient provision of hospice care. Such report shall include the feasibility and advisability of providing for prospective reimbursement for for hospice care, an evaluation of the inclusion of payment for outpatient drugs, an evaluation of the need to alter the method of reimbursement for nutritional, dietary, and bereavement counseling as

hospice care, and any recommendations for legislative changes in the hospice care reimbursement or benefit structure.

(2) The Comptroller General shall monitor and evaluate the study and the preparation of the report under paragraph (1).

(j) The Secretary of Health and Human Services shall grant waivers of the limitations imposed by section 1814(i)(2) of the Social Security Act (relating to the cap amount), section 1861(dd)(1)(G) of such Act (relating to the limitations on the frequency and number of respite care days), and section 1861(dd)(2)(A)(iv) of such Act (relating to the aggregate limit on the number of days of inpatient care), as may be necessary to allow any institution which commenced operations as a hospice prior to January 1, 1975, to participate until October 1, 1986, in a viable manner as a hospice program under title XVIII of the Social Security Act.

COVERAGE OF EXTENDED CARE SERVICES WITHOUT REGARD TO THREE-DAY PRIOR HOSPITALIZATION REQUIREMENT

SEC. 123. (a) Section 1812(a)(2) of the Social Security Act is amended by inserting "(A)" after "(2)" and by inserting before the semicolon at the end the following: ", and (B) to the extent provided in subsection (f), extended care services that are not post-hospital extended care services".

(b) Section 1812 of such Act is further amended by redesignating subsection (f) as subsection (g) and by inserting after subsection (e) the following new subsection:

"(f)(1) The Secretary shall provide for coverage, under clause (B) of subsection (a)(2), of extended care services which are not post-hospital extended care services at such time and for so long as the Secretary determines, and under such terms and conditions (described in paragraph (2)) as the Secretary finds appropriate, that the inclusion of such services will not result in any increase in the total of payments made under this title and will not alter the acute care nature of the benefit described in subsection (a)(2).

"(2) The Secretary may provide—

> *"(A) for such limitations on the scope and extent of services described in subsection (a)(2)(B) and on the categories of individuals who may be eligible to receive such services, and*
>
> *"(B) notwithstanding sections 1814, 1861(v), and 1886, for such restrictions and alternatives on the amounts and methods of payment for services described in such subsection,*

as may be necessary to carry out paragraph (1).".

PROVISION TEMPORARILY HOLDING PART B PREMIUM AT CONSTANT PERCENTAGE OF COST

SEC. 124. (a)(1) Section 1839(c)(2) of the Social Security Act is amended by striking out "except as provided in subsection (d)" and inserting in lieu thereof "except as provided in subsections (d) and (g)".

(2) Section 1839(c)(3) of such Act is amended by inserting "(except as otherwise provided in subsection (g))" after "The monthly premium shall".

(b) Section 1839 of such Act is amended by adding at the end thereof the following new subsection:

"(g)(1) Notwithstanding the provisions of subsection (c), the monthly premium for each individual enrolled under this part for each month after June 1983 and prior to July 1985 shall be an amount equal to 50 percent of the monthly actuarial rate for enrollees age 65 and over, as determined under subsection (c)(1) and applicable to such month.

"(2) Any increases in premium amounts taking effect prior to July 1985 by reason of paragraph (1) shall be taken into account for purposes of determining increases thereafter under subsection (c)(3).".

(c) Section 1844(a)(1) of such Act is amended by striking out "section 1839(c)(3)" each place it appears in subparagraphs (A)(i) and (B)(i) and inserting in lieu thereof in each instance "section 1839(c)(3) or 1839(g), as the case may be".

SPECIAL ENROLLMENT PROVISIONS FOR MERCHANT SEAMEN

SEC. 125. (a) Any individual who—

(1) was entitled to medical, surgical, and dental treatment and hospitalization under section 322(a) of the Public Health Service Act (as in effect on September 30, 1981), including such entitlement on the basis of continuing medical care under 42 C.F.R. §32.17, at any time during the period beginning on March 10, 1981, and ending on October 1, 1981, and

(2) as of September 30, 1981, was eligible under section 1818(a) or section 1836 of the Social Security Act to enroll in the insurance program established by part A or part B, respectively, of title XVIII of that Act (hereinafter in this section referred to as the "respective program"),

may enroll (if not otherwise enrolled) in the respective program during the period beginning on the first day of the first month beginning at least 20 days after the date of the enactment of this Act and ending on December 31, 1982.

(b)(1) The coverage period under the respective program of an individual who enrolls under subsection (a) shall begin—

(A) on the first day of the month following the month in which the individual enrolls, or

(B) on October 1, 1981, if the individual files a request for this subparagraph to apply and pays the monthly premiums for the months so covered.

(2) The coverage period under the respective program of an individual described in subsection (a) who enrolled in the respective program before the enrollment period described in that subsection shall be retroactively extended to October 1, 1981, if the individual files a request before January 1, 1983, for such retroactive extension and pays the monthly premiums for the months so covered.

(c)(1) For purposes of section 1839(d) of the Social Security Act with respect to the monthly premium for months after September 1981, if an individual described in subsection (a) has enrolled in the insurance program under part B of title XVIII of the Social Security Act at any time before the end of the enrollment period described in subsection (a), any month (before the end of that enrollment period) in which he was not enrolled in that program shall not be treated as a month in which he could have been enrolled in the program.

(2) Paragraph (1) shall not apply to an individual—

(A) if the individual has enrolled in the insurance program before March 10, 1981, unless the enrollment was terminated solely because the individual lost eligibility to be so enrolled, or

(B) unless the individual applies for the benefit of such paragraph before January 1, 1983.

(d)(1) The Secretary of Health and Human Services, beginning as soon as possible but not later than 30 days after the date of the enactment of this Act, shall provide for the dissemination of information—

(A) to unions and other associations representing or assisting seamen,

(B) to offices enrolling individuals under the respective programs, and

(C) to such other entities and in such a manner as will effectively inform individuals eligible for benefits under this section,

concerning the special benefits provided under this section.

(2) An individual may establish that the individual was entitled at a date to medical, surgical, and dental treatment and hospitalization under section 322(a) of the Public Health Service Act (as in effect before October 1, 1981) by providing—

(A) documentation relating to the status under which the individual was provided care in (or under arrangements with) a Public Health Service facility on that date,

(B) the individual's seamen's papers covering that date, or

(C) such other reasonable documentation as the Secretary may require.

PART III—MISCELLANEOUS PROVISIONS

EXTENDING MEDICARE PROFICIENCY EXAMINATION AUTHORITY

SEC. 126. Section 1123(a) of the Social Security Act is amended by striking out "December 31, 1981" and inserting in lieu thereof "September 30, 1983".

REGULATIONS REGARDING ACCESS TO BOOKS AND RECORDS

SEC. 127. Section 952 of the Omnibus Reconciliation Act of 1980 (94 Stat. 2646) is amended—

(1) by inserting "(a)" after "SEC. 952.", and

(2) by adding at the end the following new subsection:

"(b) Unless the Secretary of Health and Human Services first publishes final regulations prescribing the criteria and procedures described in the last sentence of section 1861(v)(1)(I) of the Social Security Act by January 1, 1983, after providing a period of not less than 60 days for public comment on proposed regulations, the amendment made by subsection (a) shall only apply to books, documents, and records relating to services furnished (pursuant to contract or subcontract) on or after the date on which final regulations of the Secretary are first published.".

TECHNICAL CORRECTIONS TO OMNIBUS BUDGET RECONCILIATION ACT OF 1981

SEC. 128. (a)(1) Section 1861(cc)(1) of the Social Security Act is amended, in the matter following subparagraph (H), by striking out "outpatient" and inserting in lieu thereof "inpatient".

(2) The second sentence of section 1862(b)(1) of such Act is amended by striking out "or plan".

(3) Section 1862(b)(2)(A) of such Act is amended by striking out "section 162(h)(2)" and inserting in lieu thereof "section 162(i)(2)".

(4) The first sentence of section 1862(b)(2)(B) of such Act is amended by inserting "furnished" before "to an individual".

(5) Section 1866(b) of such Act is amended by striking out "(and in the case of a skilled nursing facility, prior to the end of the term specified in subsection (a)(1))" in the matter preceding paragraph (1).

(6) The second subsection (c) of section 1884 of such Act is redesignated as subsection (d).

(b) Section 162 of the Internal Revenue Code of 1954 is amended—

(1) by redesignating the subsection (i) (relating to cross reference), as redesignated by the Economic Recovery Tax Act of 1981 (Public Law 95-34), as subsection (j), and

(2) by redesignating the subsection (h) (relating to group health plans), as added by section 2146(b) of the Omnibus Budget Reconciliation Act of 1981, as subsection (i).

(c)(1) Section 2143(b)(1) of the Omnibus Budget Reconciliation Act of 1981 is amended by striking out "costs" and inserting in lieu thereof "cost".

(2) Section 2203(f)(3) of such Act is amended by striking out "August 1982" and inserting in lieu thereof "August 1981".

(d)(1) Sections 1842(b)(3)(B)(ii)(II) and 1870(c) of the Social Security Act are each amended by striking out "1862" and inserting in lieu thereof "1862(a)".

(2) The final subparagraph (C) of section 1861(e) of such Act is amended by striking out "may (i)," and inserting in lieu thereof "(i) may".

(3) Section 1865(b) of such Act is amended by striking out "an institution" and "such institution" and inserting in lieu thereof "a hospital" and "the hospital", respectively.

(4) Section 1866(a)(1)(B) of such Act is amended by inserting "of section 1862(a)" after "(1) or (9)".

(e)(1) Any amendment to the Omnibus Budget Reconciliaton Act of 1981 made by this section shall be effective as if it had been originally included in the provision of the Omnibus Budget Reconciliation Act of 1981 to which such amendment relates.

(2) Except as otherwise provided in this section, any amendment to the Social Security Act or the Internal Revenue Code of 1954 made by this section (other than subsection (d)) shall be effective as if it had been originally included as a part of that provision of the Social Security Act or Internal Revenue Code of 1954 to which it relates, as such provision of such Act or Code was amended by the Omnibus Budget Reconciliaton Act of 1981.

(3) The amendments made by subsection (d) shall take effect upon enactment.

SUBTITLE B—MEDICAID

COPAYMENTS BY MEDICAID RECIPIENTS

SEC. 131. (a) Section 1902(a)(14) of the Social Security Act is amended to read as follows:

"(14) provide that enrollment fees, premiums, or similar charges, and deductions, cost sharing, or similar charges, may be imposed only as provided in section 1916;".

(b) Title XIX of the Social Security Act is amended by adding at the end thereof the following new section:

"USE OF ENROLLMENT FEES, PREMIUMS, DEDUCTIONS, COST SHARING, AND SIMILAR CHARGES

"SEC. 1916. (a) The State plan shall provide that in the case of individuals described in section 1902(a)(10)(A) who are eligible under the plan—

"(1) no enrollment fee, premium, or similar charge will be imposed under the plan;

"(2) no deduction, cost sharing or similar charge will be imposed under the plan with respect to—

"(A) services furnished to individuals under 18 years of age (and, at the option of the State, individuals under 21, 20, or 19 years of age, or any reasonable category of individuals 18 years of age or over),

"(B) services furnished to pregnant women, if such services relate to the pregnancy or to any other medical condition which may complicate the pregnancy (or, at the option of the State, any services furnished to pregnant women),

"(C) services furnished to any individual who is an inpatient in a hospital, skilled nursing facility, intermediate care facility, or other medical institution, if such individual is required, as a condition of receiving services in such institution under the State plan, to spend for costs of medical care all but a minimal amount of his income required for personal needs, or

"(D) emergency services (as defined by the Secretary), family planning services and supplies described in section 1905(a)(4)(C), or services furnished to such an individual by a health maintenance organization (as defined in section 1903(m)) in which he is enrolled;

"(3) any deduction, cost sharing, or similar charge imposed under the plan with respect to other such individuals or other care and services will be nominal in amount (as determined by the Secretary in regulations which shall, if the definition of 'nominal' under the regulations in effect on July 1, 1982 is changed, take into account the level of cash assistance provided in such State and such other criteria as the Secretary determines to be appropriate); except that a deduction, cost-sharing, or similar charge of up to twice the nominal amount established for outpatient services may be imposed by a State under a waiver granted by the Secretary for services received at a hospital emergency room if the services are not emergency services (referred to in paragraph (2)(D)) and the State has established

to the satisfaction of the Secretary that individuals eligible for services under the plan have actually available and accessible to them alternative sources of nonemergency, outpatient services.

"(b) The State plan shall provide that in the case of individuals other than those described in section 1902(a)(10)(A) who are eligible under the plan—

"(1) there may be imposed an enrollment fee, premium, or similar charge, which (as determined in accordance with standards prescribed by the Secretary) is related to the individual's income,

"(2) no deduction, cost sharing, or similar charge will be imposed under the plan with respect to—

"(A) services furnished to individuals under 18 years of age (and, at the option of the State, individuals under 21, 20, or 19 years of age, or any reasonable category of individuals 18 years of age or over),

"(B) services furnished to pregnant women, if such services relate to the pregnancy or to any other medical condition which may complicate the pregnancy (or, at the option of the State, any services furnished to pregnant women),

"(C) services furnished to any individual who is an inpatient in a hospital, skilled nursing facility, intermediate care facility, or other medical institution, if such individual is required, as a condition of receiving services in such institution under the State plan, to spend for costs of medical care all but a minimal amount of his income required for personal needs, or

"(D) emergency services (as defined by the Secretary), family planning services and supplies described in section 1905(a)(4)(C), or (at the option of the State) services furnished to such an individual by a health maintenance organization (as defined in section 1903(m)) in which he is enrolled;

"(3) any deduction, cost sharing, or similar charge imposed under the plan with respect to other such individuals or other care and services will be nominal in amount (as determined by the Secretary in regulations which shall, if the definition of 'nominal' under the regulations in effect on July 1, 1982 is changed, take into account the level of cash assistance provided in such State and such other criteria as the Secretary determines to be appropriate); except that a deduction, cost-sharing, or similar charge of up to twice the nominal amount established for outpatient services may be imposed by a State under a waiver granted by the Secretary for services received at a hospital emergency room if the services are not emergency services (referred to in paragraph (2)(D)) and the State has established to the satisfaction of the Secretary that individuals eligible for services under the plan have actually available and accessible to them alternative sources of nonemergency, outpatient services.

"(c) The State plan shall require that no provider participating under the State plan may deny care or services to an individual eligible for such care or services under the plan on account of such individual's inability to pay a deduction, cost sharing, or similar charge. The requirements of this subparagraph shall not extinguish

the liability of the individual to whom the care or services were furnished for payment of the deduction, cost sharing, or similar charge.

"(d) No deduction, cost sharing, or similar charge may be imposed under any waiver authority of the Secretary unless authorized under this section, unless such waiver is for a demonstration project which the Secretary finds after public notice and opportunity for comment—

"(1) will test a unique and previously untested use of copayments,

"(2) is limited to a period of not more than two years,

"(3) will provide benefits to recipients of medical assistance which can reasonably be expected to be equivalent to the risks to the recipients,

"(4) is based on a reasonable hypothesis which the demonstration is designed to test in a methodologically sound manner, including the use of control groups of similar recipients of medical assistance in the area, and

"(5) in which participation is voluntary, or in which provision is made for assumption of liability for preventable damage to the health of recipients of medical assistance resulting from involuntary participation.".

(b) Section 1902(a)(10) of such Act is amended in the matter following subparagraph (D)—

(1) by striking out "and" before "(III)"; and

(2) by inserting before the semicolon at the end thereof the following: "and (IV) the imposition of a deductible, cost sharing, or similar charge for any item or service furnished to an individual not eligible for the exemption under section 1916(a)(2) or (b)(2) shall not require the imposition of a deductible, cost sharing, or similar charge for the same item or service furnished to an individual who is eligible for such exemption".

(c)(1) Except as provided in paragraph (2), the amendments made by this section shall become effective on October 1, 1982.

(2) In the case of a State plan for medical assistance under title XIX of the Social Security Act which the Secretary of Health and Human Services determines requires State legislation in order for the plan to meet the additional requirements imposed by the amendments made by this section, the State plan shall not be regarded as failing to comply with the requirements of such title solely on the basis of its failure to meet these additional requirements before the first day of the first calendar quarter beginning after the close of the first regular session of the State legislature that begins after the date of the enactment of this Act.

MODIFICATIONS IN LIEN PROVISIONS

SEC. 132. (a) Section 1902(a)(18) of the Social Security Act is amended to read as follows:

"(18) comply with the provisions of section 1917 with respect to liens, adjustments and recoveries of medical assistance correctly paid, and transfers of assets;".

(b) Title XIX of such Act is amended by adding after section 1916 (added by section 131 of this Act) the following new section:

"LIENS, ADJUSTMENTS AND RECOVERIES, AND TRANSFERS OF ASSETS

"SEC. 1917. (a)(1) No lien may be imposed against the property of any individual prior to his death on account of medical assistance paid or to be paid on his behalf under the State plan, except—

"(A) pursuant to the judgment of a court on account of benefits incorrectly paid on behalf of such individual, or

"(B) in the case of the real property of an individual—

"(i) who is an inpatient in a skilled nursing facility, intermediate care facility, or other medical institution, if such individual is required, as a condition of receiving services in such institution under the State plan, to spend for costs of medical care all but a minimal amount of his income required for personal needs, and

"(ii) with respect to whom the State determines, after notice and opportunity for a hearing (in accordance with procedures established by the State), that he cannot reasonably be expected to be discharged from the medical institution and to return home,

except as provided in paragraph (2).

"(2) No lien may be imposed under paragraph (1)(B) on such individual's home if—

"(A) the spouse of such individual,

"(B) such individual's child who is under age 21, or (with respect to States eligible to participate in the State program established under title XVI) is blind or permanently and totally disabled, or (with respect to States which are not eligible to participate in such program) is blind or disabled as defined in section 1614, or

"(C) a sibling of such individual (who has an equity interest in such home and who was residing in such individual's home for a period of at least one year immediately before the date of the individual's admission to the medical institution),

is lawfully residing in such home.

"(3) Any lien imposed with respect to an individual pursuant to paragraph (1)(B) shall dissolve upon that individual's discharge from the medical institution and return home.

"(b)(1) No adjustment or recovery of any medical assistance correctly paid on behalf of an individual under the State plan may be made, except—

"(A) in the case of an individual described in subsection (a)(1)(B), from his estate or upon sale of the property subject to a lien imposed on account of medical assistance paid on behalf of such individual, and

"(B) in the case of any other individual who was 65 years of age or older when he received such assistance, from his estate.

"(2) Any adjustment or recovery under paragraph (1) may be made only after the death of the individual's surviving spouse, if any, and only at a time—

"(A) when he has no surviving child who is under age 21, or (with respect to States eligible to participate in the State program established under title XVI) is blind or permanently and totally disabled, or (with respect to States which are not eligible

to participate in such program) is blind or disabled as defined in section 1614; and

"(B) in the case of a lien on an individual's home under subsection (a)(1)(B), when—

"(i) no sibling of the individual (who was residing in the individual's home for a period of at least one year immediately before the date of the individual's admission to the medical institution), and

"(ii) no son or daughter of the individual (who was residing in the individual's home for a period of at least two years immediately before the date of the individual's admission to the medical institution, and who establishes to the satisfaction of the State that he or she provided care to such individual which permitted such individual to reside at home rather than in an institution),

is lawfully residing in such home and has lawfully resided in such home on a continuous basis since the date of the individual's admission to the medical institution.

"(c)(1) Notwithstanding any other provision of this title, an individual who would otherwise be eligible for medical assistance under the State plan approved under this title may be denied such assistance if such individual would not be eligible for such medical assistance but for the fact that he disposed of resources for less than fair market value. If the State plan provides for the denial of such assistance by reason of such disposal of resources, the State plan shall specify a procedure for implementing such denial which, except as provided in paragraph (2), is not more restrictive than the procedure specified in section 1613(c) of this Act, and which may provide for a waiver of denial of such assistance in any instance where the State determines that such denial would work an undue hardship.

"(2)(A) In any case where the uncompensated value of disposed of resources exceeds $12,000, the State plan may provide for a period of ineligibility which exceeds 24 months. If a State plan provides for a period of ineligibility exceeding 24 months, such plan shall provide for the period of ineligibility to bear a reasonable relationship to such uncompensated value.

"(B)(i) In the case of any individual who is an inpatient in a skilled nursing facility, intermediate care facility, or other medical institution. if such individual is required, as a condition of receiving services in such institution under the State plan, to spend for costs of medical care all but a minimal amount of his income required for personal needs, and, who, at any time during or after the 24-month period immediately prior to application for medical assistance under the State plan, disposed of a home for less than fair market value, the State plan (subject to clause (iii)) may provide for a period of ineligibility for medical assistance in accordance with clause (ii).

"(ii) If the State plan provides for a period of ineligibility under clause (i), such plan—

"(I) shall provide that such individual shall be ineligible for all medical assistance for a period of 24 months after the date on which he disposed of such home, except that, in the case where the uncompensated value of the home is less than the

average amount payable under the State plan as medical assistance for 24 months of care in a skilled nursing facility, the period of ineligibility shall be such shorter time as bears a reasonable relationship (based upon the average amount payable under the State plan as medical assistance for care in a skilled nursing facility) to the uncompensated value of the home, and

"(II) may provide (at the option of the State) that, in the case where the uncompensated value of the home is more than the average amount payable under the State plan as medical assistance for 24 months of care in a skilled nursing facility, such individual shall be ineligible for all medical assistance for a period in excess of 24 months after the date on which he disposed of such home which bears a reasonable relationship (based upon the average amount payable under the State plan as medical assistance for care in a skilled nursing facility) to the uncompensated value of the home.

"(iii) An individual shall not be ineligible for medical assistance by reason of clause (ii) if—

"(I) a satisfactory showing is made to the State (in accordance with any regulations promulgated by the Secretary) that the individual cannot reasonably be expected to be discharged from the medical institution and to return to that home,

"(II) title to such home was transferred to the individual's spouse or child who is under age 21, or (with respect to States eligible to participate in the State program established under title XVI) is blind or permanently and totally disabled, or (with respect to States which are not eligible to participate in such program) is blind or disabled as defined in section 1614,

"(III) a satisfactory showing is made to the State (in accordance with any regulations promulgated by the Secretary) that the individual intended to dispose of the home either at fair market value, or for other valuable consideration, or

"(IV) if the State determines that denial of eligibility would work an undue hardship.

"(3) In any case where an individual is ineligible for medical assistance under the State plan solely because of the applicability to such individual of the provisions of section 1613(c), the State plan may provide for the eligibility of such individual for medical assistance under the plan if such individual would be so eligible if the State plan requirements with respect to disposal of resources applicable under paragraphs (1) and (2) of this subsection were applied in lieu of the provisions of section 1613(c).".

(c) Section 1902 of such Act is amended by striking out subsection (j) thereof.

(d) The amendments made by this section shall become effective on the date of the enactment of this Act, but the provisions of section 1917(c)(2)(B) of the Social Security Act shall not apply with respect to a transfer of assets which took place prior to such date of enactment.

LIMITATION OF FEDERAL FINANCIAL PARTICIPATION IN ERRONEOUS MEDICAL ASSISTANCE EXPENDITURES

SEC. 133. (a) Section 1903 of the Social Security Act is amended by adding at the end thereof the following new subsection:

"(u)(1)(A) Notwithstanding subsection (a)(1), if the ratio of a State's erroneous excess payments for medical assistance (as defined in subparagraph (D)) to its total expenditures for medical assistance under the State plan approved under this title exceeds 0.03, for the period consisting of the third and fourth quarters of fiscal year 1983, or for any full fiscal year thereafter, then the Secretary shall make no payment for such period or fiscal year with respect to so much of such erroneous excess payments as exceeds such allowable error rate of 0.03.

"(B) The Secretary may waive, in certain limited cases, all or part of the reduction required under subparagraph (A) with respect to any State if such State is unable to reach the allowable error rate for a period or fiscal year despite a good faith effort by such State.

"(C) In estimating the amount to be paid to a State under subsection (d), the Secretary shall take into consideration the limitation on Federal financial participation imposed by subparagraph (A) and shall reduce the estimate he makes under subsection (d)(1), for purposes of payment to the State under subsection (d)(3), in light of any expected erroneous excess payments for medical assistance (estimated in accordance with such criteria, including sampling procedures, as he may prescribe and subject to subsequent adjustment, if necessary, under subsection (d)(2)).

"(D)(i) For purposes of this subsection, the term 'erroneous excess payments for medical assistance' means the total of—

> *"(I) payments under the State plan with respect to ineligible individuals and families, and*
>
> *"(II) overpayments on behalf of eligible individuals and families by reason of error in determining the amount of expenditures for medical care required of an individual or family as a condition of eligibility.*

"(ii) In determining the amount of erroneous excess payments for medical assistance to an ineligible individual or family under clause (i)(I), if such ineligibility is the result of an error in determining the amount of the resources of such individual or family, the amount of the erroneous excess payment shall be the smaller of (I) the amount of the payment with respect to such individual or family, or (II) the difference between the actual amount of such resources and the allowable resource level established under the State plan.

"(iii) In determining the amount of erroneous excess payments for medical assistance to an individual or family under clause (i)(II), the amount of the erroneous excess payment shall be the smaller of (I) the amount of the payment on behalf of the individual or family, or (II) the difference between the actual amount incurred for medical care by the individual or family and the amount which should have been incurred in order to establish eligibility for medical assistance.

"(E) For purposes of subparagraph (D), there shall be excluded, in determining both erroneous excess payments for medical assistance and total expenditures for medical assistance—

"(i) payments with respect to any individual whose eligibility therefor was determined exclusively by the Secretary under an agreement pursuant to section 1634 and such other classes of individuals as the Secretary may by regulation prescribe whose eligibility was determined in part under such an agreement; and

"(ii) payments made as the result of a technical error.

"(2) The State agency administering the plan approved under this title shall, at such times and in such form as the Secretary may specify, provide information on the rates of erroneous excess payments made (or expected, with respect to future periods specified by the Secretary) in connection with its administration of such plan, together with any other data he requests that are reasonably necessary for him to carry out the provisions of this subsection.

"(3)(A) If a State fails to cooperate with the Secretary in providing information necessary to carry out this subsection, the Secretary, directly or through contractual or such other arrangements as he may find appropriate, shall establish the error rates for that State on the basis of the best data reasonably available to him and in accordance with such techniques for sampling and estimating as he finds appropriate.

"(B) In any case in which it is necessary for the Secretary to exercise his authority under subparagraph (A) to determine a State's error rates for a fiscal year, the amount that would otherwise be payable to such State under this title for quarters in such year shall be reduced by the costs incurred by the Secretary in making (directly or otherwise) such determination.

"(4) This subsection shall not apply with respect to Puerto Rico, Guam, the Virgin Islands, the Northern Mariana Islands, or American Samoa.".

(b) The amendment made by subsection (a) shall become effective on the date of the enactment of this Act.

(c) No provision of law limiting Federal financial participation with respect to erroneous payments made by States under a State plan approved under title XIX of the Social Security Act (including any provision contained in, or incorporated by reference into, any appropriation Act or resolution making continuing appropriations), other than the limitations contained in section 1903 of such Act, shall be effective with respect to payments to States under such section 1903 for quarters beginning on or after October 1, 1982, unless such provision of law is enacted after the date of the date of the enactment of this Act and expressly provides that such limitation is in addition to or in lieu of the limitations contained in section 1903 of the Social Security Act.

MEDICAID COVERAGE OF HOME CARE FOR CERTAIN DISABLED CHILDREN

SEC. 134. (a) Section 1902(e) of the Social Security Act is amended by adding at the end the following new paragraph:

"(3) At the option of the State, any individual who—

"(A) is 18 years of age or younger and qualifies as a disabled individual under section 1614(a);

"(B) with respect to whom there has been a determination by the State that—

"(i) the individual requires a level of care provided in a hospital, skilled nursing facility, or intermediate care facility,

"(ii) it is appropriate to provide such care for the individual outside such an institution, and

"(iii) the estimated amount which would be expended for medical assistance for the individual for such care outside an institution is not greater than the estimated amount which would otherwise be expended for medical assistance for the individual within an appropriate institution; and

"(C) if the individual were in a medical institution, would be eligible to have a supplemental security income (or State supplemental) payment made with respect to him under title XVI,

shall be deemed, for purposes of this title only, to be an individual with respect to whom a supplemental security income payment, or State supplemental payment, respectively, is being paid under title XVI.".

(b) The amendment made by subsection (a) shall become effective on October 1, 1982.

SIX-MONTH MORATORIUM ON DEREGULATION OF SKILLED NURSING AND INTERMEDIATE CARE FACILITIES

SEC. 135. The Secretary of Health and Human Services may not promulgate any change in the regulations prescribed under—

(1) subpart K of part 405 of subchapter B (relating to medicare conditions of participation of skilled nursing facilities),

(2) so much of subpart S of part 405 of subchapter B (relating to certification procedure for providers) as relates to certification of skilled nursing facilities, and

(3) subparts C, D, and E of part 442 of subchapter C (relating to medicaid certification and requirements for skilled nursing and intermediate care facilities),

of chapter IV of title 42 of the Code of Federal Regulations until the first day of the seventh calendar month beginning after the date of the enactment of this Act unless ordered to do so by a court of competent jurisdiction.

MEDICAID PROGRAM IN AMERICAN SAMOA

SEC. 136. (a) Section 1101(a)(1) of the Social Security Act is amended by inserting "and American Samoa" after "Such term when used in title XIX also includes the Northern Mariana Islands".

(b) Section 1108(c) of such Act is amended—

(1) by striking out "and" at the end of paragraph (3);

(2) by striking out the period at the end of paragraph (4) and inserting in lieu thereof ", and"; and

(3) by adding at the end thereof the following:

"(5) American Samoa shall not exceed $750,000.".

(c) Section 1905(b)(2) of such Act is amended by striking out "and the Northern Mariana Islands" and inserting in lieu thereof "the Northern Mariana Islands, and American Samoa".

(d) Section 1902 of such Act (as amended by section 132(c) of this Act) is amended by adding at the end thereof the following new subsection:

"(j) Notwithstanding any other requirement of this title, the Secretary may waive or modify any requirement of this title with respect to the medical assistance program in American Samoa, other than a waiver of the Federal medical assistance percentage, the limitation in section 1108(c), or the requirement that payment may be made for medical assistance only with respect to amounts expended by American Samoa for care and services described in paragraphs (1) through (18) of section 1905(a).".

(e) The amendments made by this section shall become effective on October 1, 1982.

TECHNICAL CORRECTIONS FROM OMNIBUS BUDGET RECONCILIATION ACT OF 1981

SEC. 137. (a)(1) Section 2161(b) of the Ominbus Budget Reconciliation Act of 1981 is amended by striking out "Section 1902" and inserting in lieu thereof "Section 1903".

(2) Paragraphs (1) and (2) of section 2161(c) of such Act are each amended by striking out "section 1902" and inserting in lieu thereof in each instance "section 1903".

(3) Section 2171(a)(3) of such Act is amended by striking out "by striking out paragraph (C)" and inserting in lieu thereof "by striking out '(C) if medical assistance' and all that follows through the semicolon preceding 'except that' ".

(4) Section 2181(b) of such Act is amended by inserting before the period at the end thereof the following: ", except that, in the case of a State plan under title XIX of the Social Security Act which the Secretary determines requires State legislation in order to incorporate the provisions required to be included by this section into such State plan, the State plan shall not be regarded as failing to comply with the requirements of such title solely on the basis of its failure to include the provisions required to be included in such State plan by subsection (a)(2) of this section before the first day of the first calendar quarter beginning after the close of the first regular session of the State legislature that begins after the date of enactment of this Act, but the requirements previously set forth in paragraphs (1) through (3) of section 403(g) of the Social Security Act (prior to its repeal by this section) shall apply under title XIX of such Act to such State on and after October 1, 1981, whether or not the provisions required to be included by this section in the State plan under title XIX have been incorporated into such State plan".

(5) Section 2193(c)(3)(B) of such Act is amended by striking out "or X' " and inserting in lieu thereof "or XIX' ".

(b)(1) Section 501(b)(1)(D) of the Social Security Act is amended by striking out "title IV" and inserting in lieu thereof "title VI".

(2) Section 501(b)(2) of such Act is amended by striking out "section 624 of the Economic Opportunity Act of 1964" and inserting in

lieu thereof "section 673(2) of the Omnibus Budget Reconciliation Act of 1981".

(3) Section 505(2)(B) of such Act is amended by striking out "502(b)(1)" and inserting in lieu thereof "501(b)(1)".

(4) Section 505(2)(D) of such Act is amended by striking out "the State imposes any charges" and inserting in lieu thereof "any charges are imposed".

(5) Section 1134(4) of such Act is amended by striking out "scale" and inserting in lieu thereof "sale".

(6) The heading of title XVI of such Act as such title applies in the case of Puerto Rico, Guam, and the Virgin Islands is amended by striking out ", OR FOR SUCH AID FOR THE AGED".

(7) Section 1902(a)(10)(A) of such Act is amended to read as follows:

"(A) for making medical assistance available, including at least the care and services listed in paragraphs (1) through (5) and (17) of section 1905(a), to—

"(i) all individuals receiving aid or assistance under any plan of the State approved under title I, X, XIV, or XVI, or part A or part E of title IV (including pregnant women deemed by the State to be receiving such aid as authorized in section 406(g) and individuals considered by the State to be receiving such aid as authorized under section 414(g)), or with respect to whom supplemental security income benefits are being paid under title XVI; and

"(ii) at the option of the State, to any group or groups of individuals described in section 1905(a) (or, in the case of individuals described in section 1905(a)(i), to any reasonable categories of such individuals) who are not individuals described in clause (i) of this subparagraph but—

"(I) who meet the income and resources requirements of the appropriate State plan described in clause (i) or the supplemental security income program (as the case may be),

"(II) who would meet the income and resources requirements of the appropriate State plan described in clause (i) if their work-related child care costs were paid from their earnings rather than by a State agency as a service expenditure,

"(III) who would be eligible to receive aid under the appropriate State plan described in clause (i) if coverage under such plan was as broad as allowed under Federal law,

"(IV) with respect to whom there is being paid, or who are eligible, or would be eligible if they were not in a medical institution, to have paid with respect to them, aid or assistance under the appropriate State plan described in clause (i), supplemental security income benefits under title XVI, or a State supplementary payment;

"(V) who are in a medical institution, who meet the resource requirements of the appropriate State plan described in clause (i) or the supplemental security income program, and whose income does not exceed a

separate income standard established by the State which is consistent with the limit established under section 1903(f)(4)(C), or

"(VI) who would be eligible under the State plan under this title if they were in a medical institution, with respect to whom there has been a determination that but for the provision of home or community-based services described in section 1915(c) they would require the level of care provided in a hospital, skilled nursing facility or intermediate care facility the cost of which could be reimbursed under the State plan, and who will receive home or community-based services pursuant to a waiver granted by the Secretary under section 1915(c);".

(8) Section 1902(a)(10)(C)(i) of such Act is amended—

(A) by striking out "and (II)" and inserting in lieu thereof ", (II)"; and

(B) by inserting before the semicolon at the end thereof ", and (III) the single standard to be employed in determining income and resource eligibility for all such groups, and the methodology to be employed in determining such eligibility, which shall be the same methodology which would be employed under the supplemental security income program in the case of groups consisting of aged, blind, or disabled individuals in a State in which such program is in effect, and which shall be the same methodology which would be employed under the appropriate State plan (described in subparagraph (A)(i)) to which such group is most closely categorically related in the case of other groups".

(9) Section 1902(a)(10)(C)(ii)(I) of such Act is amended by striking out "described in section 1905(a)(i)" and inserting in lieu thereof "under the age of 18 who (but for income and resources) would be eligible for medical assistance as an individual described in subparagraph (A)(i)".

(10) Section 1902(b) of such Act is amended by striking out paragraph (2) and redesignating paragraphs (3) and (4) as paragraphs (2) and (3), respectively.

(11) Section 1903(g)(1) of such Act is amended by inserting "or which is a qualified health maintenance organization (as defined in section 1310(d) of the Public Health Service Act)" after "as defined in section 1876".

(12) Section 1903(g)(1)(A) of such Act is amended by striking out "intermediate care facility services described in section 1905(d)" and inserting in lieu thereof "intermediate care facility services provided in an institution for the mentally retarded".

(13) Section 1903(k) of such Act is amended by striking out "section 1876" and inserting in lieu thereof "subsection (m) of this section".

(14) Section 1903(m)(2)(A) of such Act is amended—

(A) by striking out "and" before "(II)" in clause (iv) and inserting in lieu thereof "or"; and

(B) by striking out "unforseen" in clause (vii) and inserting in lieu thereof "unforeseen".

(15) Section 1903(s) of such Act is amended—

(A) in paragraph (1)(A), by striking out "made before fiscal year 1981" and inserting in lieu thereof "made before fiscal year 1982";

(B) in paragraph (1)(A), by striking out "without regard to payments under subsection (t) and" and inserting in lieu thereof "without regard to payments under subsections (a)(6) and (t), without regard to payments for claims relating to expenditures made for medical assistance for services received through a facility of the Indian Health Service, and";

(C) in paragraph (1)(C), by inserting "a program in operation under" before "a plan approved under this title";

(D) in paragraph (3)(D)—

(i) by striking out "determines that" and inserting in lieu thereof "must determine that";

(ii) by striking out "most recent calendar year" and inserting in lieu thereof "most recent year (which shall consist of a 12-month period determined by the Secretary for this purpose)";

(iii) by striking out "2 or 3 calendar year period" and inserting in lieu thereof "2- or 3-year period"; and

(iv) by striking out "calendar" each place it appears;

(E) in paragraph (4)(B), by inserting "and paragraph (3)(D)" after "subparagraph (A)"; and

(F) in paragraph (5)(A)(i), by inserting "(including amounts saved, to the extent such amounts can be documented to the satisfaction of the Secretary, by reason of the suspension or termination of a provider or other person for fraud or abuse, but only during the period of such suspension or termination or, if shorter, the 1-year period beginning on the date of such termination or suspension)" after "recovered or diverted".

(16) Section 1903(t) of such Act (as added by section 2161(b) of the Omnibus Budget Reconciliation Act of 1981 as amended by subsection (a) of this section) is amended—

(A) in paragraphs (1)(A) and (2)(A), by striking out "other than interest paid under subsection (d)(5)" each place it appears and inserting in lieu thereof in each instance "other than payments under subsection (a)(6), interest paid under subsection (d)(5), and payments for claims relating to expenditures made for medical assistance for services received through a facility of the Indian Health Service";

(B) in paragraph (1)(B), by striking out "between September 1982 and September 1983" and inserting in lieu thereof "for the 12-month period ending on September 30, 1983";

(C) in paragraph (1)(C), by striking out "between September 1982 and September 1984" and inserting in lieu thereof "for the 24-month period ending on September 30, 1984";

(D) in subparagraphs (B) and (C) of paragraph (1), by striking out "consumer price index for all urban consumers (published by the Bureau of Labor Statistics)" each place it appears and inserting in lieu thereof in each instance "Consumer Price Index for all urban consumers (U.S. city average) published by the Bureau of Labor Statistics"; and

(E) by amending paragraph (3) to read as follows:

"(3) Only for the purpose of computing under this subsection the Federal share of expenditures for a State for fiscal years 1982, 1983, and 1984 (in the case of the payment which may be made for the first quarter of fiscal years 1983, 1984, and 1985, respectively), the Federal medical assistance percentage for fiscal years 1982, 1983, and 1984 shall be the Federal medical assistance percentage for States in effect for fiscal year 1981, disregarding any change in such percentage after fiscal year 1981.".

(17) Section 1905(a)(i) of such Act is amended by striking out "or any reasonable category of such individuals,".

(18) Section 1905(a) of such Act is amended by striking out "or" at the end of clause (vi), inserting "or" at the end of clause (vii), and inserting after clause (vii) the following:

"(viii) pregnant women,".

(19)(A) Section 1915(b) of such Act is amended by striking out "and section 1903(m)".

(B) The amendment made by subparagraph (A) shall not apply with respect to any waiver if such waiver was granted, and the arrangement covered by the waiver was in place, prior to August 10, 1982.

(20) Section 1915(b)(1) of such Act is amended—

(A) by inserting "primary care" before "case-management system"; and

(B) by striking out "primary care services" and inserting in lieu thereof "medical care services".

(21) Section 1915(c)(1) of such Act is amended by inserting "payment for part or all of the cost of" after "may include as 'medical assistance' under such plan".

(22) Section 1915(c)(2)(B) of such Act is amended to read as follows:

"(B) the State will provide, with respect to individuals who—

"(i) are entitled to medical assistance for skilled nursing facility or intermediate care facility services under the State plan,

"(ii) may require such services, and

"(iii) may be eligible for such home or community-based care under such waiver,

for an evaluation of the need for such services;".

(23) Section 1915(c)(3) of such Act is amended—

(A) by striking out "subsection (a)(1)" and inserting in lieu thereof "section 1902(a)(1)"; and

(B) by striking out "subsection (a)(10) of section 1902" and inserting in lieu thereof "section 1902(a)(10)".

(24) Section 1915(c)(4) of such Act is amended by striking out "this section" and inserting in lieu thereof "this subsection".

(25) Section 1915(f) of such Act is amended by inserting "approval of" before "a proposed State plan".

(26) Subsection (a) of section 1128A of such Act is amended by striking out all that precedes "shall be subject" and inserting in lieu thereof the following:

"(a) Any person (including an organization, agency, or other entity) that—

"(1) presents or causes to be presented to an officer, employee, or agent of the United States, or of any department or agency

thereof, or of any State agency (as defined in subsection (h)(1)), a claim (as defined in subsection (h)(2)) that the Secretary determines is for a medical or other item or service—

"(A) that the person knows or has reason to know was not provided as claimed, or

"(B) payment for which may not be made under the program under which such claim was made, pursuant to a determination by the Secretary under section 1128, 1160(b), or 1862(d), or pursuant to a determination by the Secretary under section 1866(b)(2) with respect to which the Secretary has initiated termination proceedings; or

"(2) presents or causes to be presented to any person a request for payment which is in violation of the terms of (A) an assignment under section 1842(b)(3)(B)(ii), or (B) an agreement with a State agency not to charge a person for an item or service in excess of the amount permitted to be charged,".

(27) Section 1903(s)(5)(B) of such Act is amended by inserting "or quarters" after "carried forward to the following quarter".

(c)(1) Section 914(b)(2)(A) of the Omnibus Reconciliation Act of 1980 is amended by striking out "medical assistance" and all that follows and inserting in lieu thereof "cost reporting periods, beginning on or after April 1, 1981, of an entity providing services under a State plan approved under title XIX of the Social Security Act.".

(2) Section 914(c)(2) of the Omnibus Reconciliation Act of 1980 is amended by striking out "services provided" and all that follows and inserting in lieu thereof "cost reporting periods, beginning on or after April 1, 1981, of an entity providing services under a State plan approved under title V of the Social Security Act.".

(d)(1) Except as otherwise provided in this section, any amendment to the Omnibus Budget Reconciliation Act of 1981 made by this section shall be effective as if it had been originally included in the provision of the Omnibus Budget Reconciliation Act of 1981 to which such amendment relates.

(2) Except as otherwise provided in this section, any amendment to the Social Security Act made by the preceding provisions of this section shall be effective as if it had been originally included as a part of that provision of the Social Security Act to which it relates, as such provision of the Social Security Act was amended by the Omnibus Budget Reconciliation Act of 1981.

(e) Section 1902(a) of the Social Security Act is amended in the matter following paragraph (44) by inserting ", (26)" after "(9)(A)".

(f) Section 1905(h)(1)(C) of the Social Security Act is amended by redesignating clauses (i) and (ii) as subclauses (I) and (II) respectively, and by redesignating clauses (A) and (B) as clauses (i) and (ii) respectively.

(g) Effective October 1, 1982, section 1903(f)(3) of the Social Security Act is amended by striking out "(without regard to section 408)".

SUBTITLE C—UTILIZATION AND QUALITY CONTROL PEER REVIEW

SHORT TITLE OF SUBTITLE

SEC. 141. This subtitle may be cited as the "Peer Review Improvement Act of 1982".

REQUIREMENT FOR SECRETARY TO ENTER INTO CONTRACTS

SEC. 142. Section 1862 of the Social Security Act is amended by adding at the end thereof the following new subsection:

"(g) The Secretary shall, in making the determinations under paragraphs (1) and (9) of subsection (a), and for the purposes of promoting the effective, efficient, and economical delivery of health care services, and of promoting the quality of services of the type for which payment may be made under this title, enter into contracts with utilization and quality control peer review organizations pursuant to part B of title XI of this Act.".

ESTABLISHMENT OF UTILIZATION AND QUALITY CONTROL PEER REVIEW PROGRAM

SEC. 143. Part B of title XI of the Social Security Act is amended to read as follows:

"PART B—PEER REVIEW OF THE UTILIZATION AND QUALITY OF HEALTH CARE SERVICES

"PURPOSE

"SEC. 1151. The purpose of this part is to establish the contracting process which the Secretary must follow pursuant to the requirements of section 1862(g) of this Act, including the definition of the utilization and quality control peer review organizations with which the Secretary shall contract, the functions such peer review organizations are to perform, the confidentiality of medical records, and related administrative matters to facilitate the carrying out of the purposes of this part.

"DEFINITION OF UTILIZATION AND QUALITY CONTROL PEER REVIEW ORGANIZATION

"SEC. 1152. The term 'utilization and quality control peer review organization' means an entity which—

"(1)(A) is composed of a substantial number of the licensed doctors of medicine and osteopathy engaged in the practice of medicine or surgery in the area and who are representative of the practicing physicians in the area, designated by the Secretary under section 1153, with respect to which the entity shall perform services under this part, or (B) has available to it, by arrangement or otherwise, the services of a sufficient number of licensed doctors of medicine or osteopathy engaged in the practice of medicine or surgery in such area to assure that adequate peer review of the services provided by the various medical specialties and subspecialties can be assured; and

"(2) is able, in the judgment of the Secretary, to perform review functions required under section 1154 in a manner con-

sistent with the efficient and effective administration of this part and to perform reviews of the pattern of quality of care in an area of medical practice where actual performance is measured against objective criteria which define acceptable and adequate practice.

"CONTRACTS WITH UTILIZATION AND QUALITY CONTROL PEER REVIEW ORGANIZATIONS

"SEC. 1153. (a)(1) The Secretary shall establish throughout the United States geographic areas with respect to which contracts under this part will be made. In establishing such areas, the Secretary shall use the same areas as established under section 1152 of this Act as in effect immediately prior to the date of the enactment of the Peer Review Improvement Act of 1982, but subject to the provisions of paragraph (2).

"(2) As soon as practicable after the date of the enactment of the Peer Review Improvement Act of 1982, the Secretary shall consolidate such geographic areas, taking into account the following criteria:

"(A) Each State shall generally be designated as a geographic area for purposes of paragraph (1).

"(B) The Secretary shall establish local or regional areas rather than State areas only where the volume of review activity or other relevant factors (as determined by the Secretary) warrant such an establishment, and the Secretary determines that review activity can be carried out with equal or greater efficiency by establishing such local or regional areas. In applying this subparagraph the Secretary shall take into account the number of hospital admissions within each State for which payment may be made under title XVIII or a State plan approved under title XIX, with any State having fewer than 180,000 such admissions annually being established as a single statewide area, and no local or regional area being established which has fewer than 60,000 total hospital admissions (including public and private pay patients) under review annually, unless the Secretary determines that other relevant factors warrant otherwise.

"(C) No local or regional area shall be designated which is not a self-contained medical service area, having a full spectrum of services, including medical specialists' services.

"(b)(1) The Secretary shall enter into a contract with a utilization and quality control peer review organization for each area established under subsection (a) if a qualified organization is available in such area and such organization and the Secretary have negotiated a proposed contract which the Secretary determines will be carried out by such organization in a manner consistent with the efficient and effective administration of this part. If more than one such qualified organization meets the requirements of the preceding sentence, priority shall be given to any such organization which is described in section 1152(1)(A).

"(2)(A) During the first twelve months in which the Secretary is entering into contracts under this section, the Secretary shall not enter into a contract under this part with any entity which is, or is

affiliated with (through management, ownership, or common control), an entity which directly or indirectly makes payments to any practitioner or provider whose health care services are reviewed by such entity or would be reviewed by such entity if it entered into a contract with the Secretary under this part.

"(B) If, after the expiration of the twelve-month period referred to in subparagraph (A), the Secretary determines that there is no other entity available for an area with which the Secretary can enter into a contract under this part, the Secretary may then enter into a contract under this part with an entity described in subparagraph (A) for such area if such entity otherwise meets the requirements of this part.

"(3) The Secretary shall not enter into a contract under this part with any entity which is, or is affiliated with (through management, ownership, or common control), a health care facility, or association of such facilities, within the area served by such entity or which would be served by such entity if it entered into a contract with the Secretary under this part.

"(c) Each contract with an organization under this section shall provide that—

"(1) the organization shall perform the functions set forth in section 1154(a), or may subcontract for the performance of all or some of such functions (and for purposes of paragraphs (2) and (3) of subsection (b), a subcontract under this paragraph shall not constitute an affiliation with the subcontractor);

"(2) the Secretary shall have the right to evaluate the quality and effectiveness of the organization in carrying out the functions specified in the contract;

"(3) the contract shall be for an initial term of two years and shall be renewable on a biennial basis thereafter;

"(4) if the Secretary intends not to renew a contract, he shall notify the organization of his decision at least 90 days prior to the expiration of the contract term, and shall provide the organization an opportunity to present data, interpretations of data, and other information pertinent to its performance under the contract, which shall be reviewed in a timely manner by the Secretary;

"(5) the organization may terminate the contract upon 90 days notice to the Secretary;

"(6) the Secretary may terminate the contract prior to the expiration of the contract term upon 90 days notice to the organization if the Secretary determines that—

"(A) the organization does not substantially meet the requirements of section 1152; or

"(B) the organization has failed substantially to carry out the contract or is carrying out the contract in a manner inconsistent with the efficient and effective administration of this part, but only after such organization has had an opportunity to submit data and have such data reviewed by the panel established under subsection (d);

"(7) the Secretary shall include in the contract negotiated objectives against which the organization's performance will be judged, and negotiated specifications for use of regional norms,

or modifications thereof based on national norms, for performing review functions under the contract; and

"(8) reimbursement shall be made to the organization in accordance with the terms of the contract.

"(d)(1) Prior to making any termination under subsection (c)(5)(B), the Secretary must provide the organization with an opportunity to provide data, interpretations of data, and other information pertinent to its performance under the contract. Such data and other information shall be reviewed in a timely manner by a panel appointed by the Secretary, and the panel shall submit a report of its findings to the Secretary in a timely manner. The Secretary shall make a copy of the report available to the organization.

"(2) The Secretary may accept or not accept the findings of the panel. After the panel has submitted a report with respect to an organization, the Secretary may, with the concurrence of the organization, amend the contract to modify the scope of the functions to be carried out by the organization, or in any other manner. The Secretary may terminate a contract under the authority of subsection (c)(5)(C) upon 90 days notice after the panel has submitted a report, or earlier if the organization so agrees.

"(3) A panel appointed by the Secretary under this subsection shall consist of not more than five individuals, each of whom shall be a member of a utilization and quality control peer review organization having a contract with the Secretary under this part. While serving on such panel individuals shall be paid at a per diem rate not to exceed the current per diem equivalent at the time that service on the panel is rendered for grade GS-18 under section 5332 of title 5, United States Code. Appointments shall be made without regard to title 5, United States Code.

"(e) Contracting authority of the Secretary under this section may be carried out without regard to any provision of law relating to the making, performance, amendment, or modification of contracts of the United States as the Secretary may determine to be inconsistent with the purposes of this part. The Secretary may use different contracting methods with respect to different geographical areas.

"(f) Any determination by the Secretary to terminate or not to renew a contract under this section shall not be subject to judicial review.

"FUNCTIONS OF PEER REVIEW ORGANIZATIONS

"SEC. 1154. (a) Any utilization and quality control peer review organization entering into a contract with the Secretary under this part must perform the following functions:

"(1) The organization shall review some or all of the professional activities in the area, subject to the terms of the contract, of physicians and other health care practitioners and institutional and noninstitutional providers of health care services in the provision of health care services and items for which payment may be made (in whole or in part) under title XVIII for the purpose of determining whether—

"(A) such services and items are or were reasonable and medically necessary or otherwise allowable under section 1862(a)(1);

"(B) the quality of such services meets professionally recognized standards of health care; and

"(C) in case such services and items are proposed to be provided in a hospital or other health care facility on an inpatient basis, such services and items could, consistent with the provision of appropriate medical care, be effectively provided more economically on an outpatient basis or in an inpatient health care facility of a different type.

"(2) The organization shall determine, on the basis of the review carried out under subparagraphs (A) and (C) of paragraph (1), whether payment shall be made for services under title XVIII. Such determination shall constitute the conclusive determination on those issues for purposes of payment under title XVIII, except that payment may be made if—

"(A) such payment is allowed by reason of section 1879;

"(B) in the case of inpatient hospital services or posthospital extended care services, the peer review organization determines that additional time is required in order to arrange for postdischarge care, but payment may be continued under this subparagraph for not more than two days, but only in the case where the provider of such services did not know and could not reasonably have been expected to know (as determined under section 1879) that payment would not otherwise be made for such services under title XVIII prior to notification by the organization under paragraph (3);

"(C) such determination is changed as the result of any hearing or review of the determination under section 1155; or

"(D) such payment is authorized under section 1861(v)(1)(G).

"(3) Whenever the organization makes a determination that any health care services or items furnished or to be furnished to a patient by any practitioner or provider are disapproved, the organization shall promptly notify such practitioner or provider, such patient, and the agency or organization responsible for the payment of claims under title XVIII of this Act. In the case of practitioners and providers of services, the organization shall provide an opportunity for discussion and review of the determination.

"(4) The organization shall, after consultation with the Secretary, determine the types and kinds of cases (whether by type of health care or diagnosis involved, or whether in terms of other relevant criteria relating to the provision of health care services) with respect to which such organization will, in order to most effectively carry out the purposes of this part, exercise review authority under the contract. The organization shall notify the Secretary periodically with respect to such determinations.

"(5) The organization shall consult with nurses and other professional health care practitioners (other than physicians described in section 1861(r)(1)) and with representatives of institutional and noninstitutional providers of health care services, with respect to the organization's responsibility for the review

under paragraph (1) of the professional activities of such practitioners and providers.

"(6) The organization shall, consistent with the provisions of its contract under this part, apply professionally developed norms of care, diagnosis, and treatment based upon typical patterns of practice within the geographic area served by the organization as principal points of evaluation and review, taking into consideration national norms where appropriate. Such norms with respect to treatment for particular illnesses or health conditions shall include—

"(A) the types and extent of the health care services which, taking into account differing, but acceptable, modes of treatment and methods of organizing and delivering care, are considered within the range of appropriate diagnosis and treatment of such illness or health condition, consistent with professionally recognized and accepted patterns of care; and

"(B) the type of health care facility which is considered, consistent with such standards, to be the type in which health care services which are medically appropriate for such illness or condition can most economically be provided.

"(7) The organization, to the extent necessary and appropriate to the performance of the contract, shall—

"(A) make arrangements to utilize the services of persons who are practitioners of, or specialists in, the various areas of medicine (including dentistry), or other types of health care, which persons shall, to the maximum extent practicable, be individuals engaged in the practice of their profession within the area served by such organization;

"(B) undertake such professional inquiries either before or after, or both before and after, the provision of services with respect to which such organization has a responsibility for review which in the judgment of such organization will facilitate its activities;

"(C) examine the pertinent records of any practitioner or provider of health care services providing services with respect to which such organization has a responsibility for review under paragraph (1); and

"(D) inspect the facilities in which care is rendered or services are provided (which are located in such area) of any practitioner or provider of health care services providing services with respect to which such organization has a responsibility for review under paragraph (1).

"(8) The organization shall perform such duties and functions and assume such responsibilities and comply with such other requirements as may be required by this part or under regulations of the Secretary promulgated to carry out the provisions of this part.

"(9) The organization shall collect such information relevant to its functions, and keep and maintain such records, in such form as the Secretary may require to carry out the purposes of this part, and shall permit access to and use of any such infor-

mation and records as the Secretary may require for such purposes, subject to the provisions of section 1160.

"(10) The organization shall coordinate activities, including information exchanges, which are consistent with economical and efficient operation of programs among appropriate public and private agencies or organizations including—

"(A) agencies under contract pursuant to sections 1816 and 1842 of this Act;

"(B) other peer review organizations having contracts under this part; and

"(C) other public or private review organizations as may be appropriate.

"(11) The organization shall make available its facilities and resources for contracting with private and public entities paying for health care in its area for review, as feasible and appropriate, of services reimbursed by such entities.

"(b)(1) No physician shall be permitted to review—

"(A) health care services provided to a patient if he was directly responsible for providing such services; or

"(B) health care services provided in or by an institution, organization, or agency, if he or any member of his family has, directly or indirectly, a significant financial interest in such institution, organization, or agency.

"(2) For purposes of this subsection, a physician's family includes only his spouse (other than a spouse who is legally separated from him under a decree of divorce or separate maintenance), children (including legally adopted children), grandchildren, parents, and grandparents.

"(c) No utilization and quality control peer review organization shall utilize the services of any individual who is not a duly licensed doctor of medicine, osteopathy, or dentistry to make final determinations of denial decisions in accordance with its duties and functions under this part with respect to the professional conduct of any other duly licensed doctor of medicine, osteopathy, or dentistry, or any act performed by any duly licensed doctor of medicine, osteopathy, or dentistry in the exercise of his profession.

"RIGHT TO HEARING AND JUDICIAL REVIEW

"SEC. 1155. Any beneficiary who is entitled to benefits under title XVIII, and any practitioner or provider, who is dissatisfied with a determination made by a contracting peer review organization in conducting its review responsibilities under this part, shall be entitled to a reconsideration of such determination by the reviewing organization. Where the reconsideration is adverse to the beneficiary and where the matter in controversy is $200 or more, such beneficiary shall be entitled to a hearing by the Secretary (to the same extent as is provided in section 205(b)), and, where the amount in controversy is $2,000 or more, to judicial review of the Secretary's final decision.

"OBLIGATIONS OF HEALTH CARE PRACTITIONERS AND PROVIDERS OF HEALTH CARE SERVICES; SANCTIONS AND PENALTIES; HEARINGS AND REVIEW

"SEC. 1156. (a) It shall be the obligation of any health care practitioner and any other person (including a hospital or other health care facility, organization, or agency) who provides health care services for which payment may be made (in whole or in part) under title XVIII, to assure, to the extent of his authority that services or items ordered or provided by such practitioner or person to beneficiaries and recipients under such title—

"(1) will be provided economically and only when, and to the extent, medically necessary;

"(2) will be of a quality which meets professionally recognized standards of health care; and

"(3) will be supported by evidence of medical necessity and quality in such form and fashion and at such time as may reasonably be required by a reviewing peer review organization in the exercise of its duties and responsibilities.

"(b)(1) If after reasonable notice and opportunity for discussion with the practitioner or person concerned, any organization having a contract with the Secretary under this part determines that such practitioner or person has—

"(A) failed in a substantial number of cases substantially to comply with any obligation imposed on him under subsection (a), or

"(B) grossly and flagrantly violated any such obligation in one or more instances,

such organization shall submit a report and recommendations to the Secretary. If the Secretary agrees with such determination, and determines that such practitioner or person, in providing health care services over which such organization has review responsibility and for which payment (in whole or in part) may be made under title XVIII, has demonstrated an unwillingness or a lack of ability substantially to comply with such obligations, the Secretary (in addition to any other sanction provided under law) may exclude (permanently or for such period as the Secretary may prescribe) such practitioner or person from eligibility to provide such services on a reimbursable basis. If the Secretary fails to act upon the recommendations submitted to him by such organization within 120 days after such submission, such practitioner or person shall be excluded from eligibility to provide services on a reimbursable basis until such time as the Secretary determines otherwise.

"(2) A determination made by the Secretary under this subsection to exclude a practitioner or person shall be effective at such time and upon such reasonable notice to the public and to the practitioner or person furnishing the services involved as may be specified in regulations. Such determination shall be effective with respect to services furnished to an individual on or after the effective date of such determination (except that in the case of institutional health care services such determination shall be effective in the manner provided in title XVIII with respect to terminations of provider agreements), and shall remain in effect until the Secretary finds and gives reasonable notice to the public that the basis for such de-

termination has been removed and that there is reasonable assurance that it will not recur.

"*(3) In lieu of the sanction authorized by paragraph (1), the Secretary may require that (as a condition to the continued eligibility of such practitioner or person to provide such health care services on a reimbursable basis) such practitioner or person pays to the United States, in case such acts or conduct involved the provision or ordering by such practitioner or person of health care services which were medically improper or unnecessary, an amount not in excess of the actual or estimated cost of the medically improper or unnecessary services so provided. Such amount may be deducted from any sums owing by the United States (or any instrumentality thereof) to the practitioner or person from whom such amount is claimed.*

"*(4) Any practitioner or person furnishing services described in paragraph (1) who is dissatisfied with a determination made by the Secretary under this subsection shall be entitled to reasonable notice and opportunity for a hearing thereon by the Secretary to the same extent as is provided in section 205(b), and to judicial review of the Secretary's final decision after such hearing as is provided in section 205(g).*

"*(c) It shall be the duty of each utilization and quality control peer review organization to use such authority or influence it may possess as a professional organization, and to enlist the support of any other professional or governmental organization having influence or authority over health care practitioners and any other person (including a hospital or other health care facility, organization, or agency) providing health care services in the area served by such review organization, in assuring that each practitioner or person (referred to in subsection (a)) providing health care services in such area shall comply with all obligations imposed on him under subsection (a).*

"*LIMITATION ON LIABILITY*

"*SEC. 1157. (a) Notwithstanding any other provision of law, no person providing information to any organization having a contract with the Secretary under this part shall be held, by reason of having provided such information, to have violated any criminal law, or to be civilly liable under any law of the United States or of any State (or political subdivision thereof) unless—*

"*(1) such information is unrelated to the performance of the contract of such organization; or*

"*(2) such information is false and the person providing it knew, or had reason to believe, that such information was false.*

"*(b) No person who is employed by, or who has a fiduciary relationship with, any such organization or who furnishes professional services to such organization, shall be held by reason of the performance by him of any duty, function, or activity required or authorized pursuant to this part or to a valid contract entered into under this part, to have violated any criminal law, or to be civilly liable under any law of the United States or of any State (or political subdivision thereof) provided he has exercised due care.*

"*(c) No doctor of medicine or osteopathy and no provider (including directors, trustees, employees, or officials thereof) of health care* *services shall be civilly liable to any person under any law of the United States or of any State (or political subdivision thereof) on account of any action taken by him in compliance with or reliance upon professionally developed norms of care and treatment applied by an organization under contract pursuant to section 1153 operating in the area where such doctor of medicine or osteopathy or provider took such action; but only if—*

"(1) he takes such action in the exercise of his profession as a doctor of medicine or osteopathy or in the exercise of his functions as a provider of health care services; and

"(2) he exercised due care in all professional conduct taken or directed by him and reasonably related to, and resulting from, the actions taken in compliance with or reliance upon such professionally accepted norms of care and treatment.

"(d) The Secretary shall make payment to an organization under contract with him pursuant to this part, or to any member or employee thereof, or to any person who furnishes legal counsel or services to such organization, in an amount equal to the reasonable amount of the expenses incurred, as determined by the Secretary, in connection with the defense of any suit, action, or proceeding brought against such organization, member, or employee related to the performance of any duty or function under such contract by such organization, member, or employee.

"APPLICATION OF THIS PART TO CERTAIN STATE PROGRAMS RECEIVING FEDERAL FINANCIAL ASSISTANCE

"SEC. 1158. (a) A State plan approved under title XIX of this Act may provide that the functions specified in section 1154 may be performed in an area by contract with a utilization and quality control peer review organization that has entered into a contract with the Secretary in accordance with the provisions of section 1862(g).

"(b) In the event a State enters into a contract in accordance with subsection (a), the Federal share of the expenditures made to the contracting organization for its costs in the performance of its functions under the State plan shall be 75 percent (as provided in section 1903(a)(3)(C)).

"AUTHORIZATION FOR USE OF CERTAIN FUNDS TO ADMINISTER THE PROVISIONS OF THIS PART

"SEC. 1159. Expenses incurred in the administration of the contracts described in section 1862(g) shall be payable from—

"(1) funds in the Federal Hospital Insurance Trust Fund; and

"(2) funds in the Federal Supplementary Medical Insurance Trust Fund,

in such amounts from each of such Trust Funds as the Secretary shall deem to be fair and equitable after taking into consideration the expenses attributable to the administration of this part with respect to each of such programs. The Secretary shall make such transfers of moneys between such Trust Funds as may be appropriate to settle accounts between them in cases where expenses properly payable from one such Trust Fund have been paid from the other such Trust Fund.

"PROHIBITION AGAINST DISCLOSURE OF INFORMATION

"SEC. 1160. (a) An organization, in carrying out its functions under a contract entered into under this part, shall not be a Federal agency for purposes of the provisions of section 552 of title 5, United States Code (commonly referred to as the Freedom of Information Act). Any data or information acquired by any such organization in the exercise of its duties and functions shall be held in confidence and shall not be disclosed to any person except—

"(1) to the extent that may be necessary to carry out the purposes of this part,

"(2) in such cases and under such circumstances as the Secretary shall by regulations provide to assure adequate protection of the rights and interests of patients, health care practitioners, or providers of health care, or

"(3) in accordance with subsection (b).

"(b) An organization having a contract with the Secretary under this part shall provide in accordance with procedures and safeguards established by the Secretary, data and information—

"(1) which may identify specific providers or practitioners as may be necessary—

"(A) to assist Federal and State agencies recognized by the Secretary as having responsibility for identifying and investigating cases or patterns of fraud or abuse, which data and information shall be provided by the peer review organization to any such agency at the request of such agency relating to a specific case or pattern;

"(B) to assist appropriate Federal and State agencies recognized by the Secretary as having responsibility for identifying cases or patterns involving risks to the public health, which data and information shall be provided by the peer review organization to any such agency—

"(i) at the discretion of the peer review organization, at the request of such agency relating to a specific case or pattern with respect to which such agency has made a finding, or has a reasonable belief, that there may be a substantial risk to the public health, or

"(ii) upon a finding by, or the reasonable belief of, the peer review organization that there may be a substantial risk to the public health; and

"(C) to assist appropriate State agencies recognized by the Secretary as having responsibility for licensing or certification of providers or practitioners, which data and information shall be provided by the peer review organization to any such agency at the request of such agency relating to a specific case, but only to the extent that such data and information is required by the agency in carrying out a function which is within the jurisdiction of such agency under State law; and

"(2) to assist the Secretary, and such Federal and State agencies recognized by the Secretary as having health planning or related responsibilities under Federal or State law (including health systems agencies and State health planning and development agencies), in carrying out appropriate health care plan-

ning and related activities, which data and information shall be provided in such format and manner as may be prescribed by the Secretary or agreed upon by the responsible Federal and State agencies and such organization, and shall be in the form of aggregate statistical data (without explicitly identifying any individual) on a geographic, institutional, or other basis reflecting the volume and frequency of services furnished, as well as the demographic characteristics of the population subject to review by such organization.

The penalty provided in subsection (c) shall not apply to the disclosure of any information received under this subsection, except that such penalty shall apply to the disclosure (by the agency receiving such information) of any such information described in paragraph (1) unless such disclosure is made in a judicial, administrative, or other formal legal proceeding resulting from an investigation conducted by the agency receiving the information. An organization may require payment of a reasonable fee for providing information under this subsection in response to a request for such information.

"(c) It shall be unlawful for any person to disclose any such information described in subsection (a) other than for the purposes provided in subsections (a) and (b), and any person violating the provisions of this section shall, upon conviction, be fined not more than $1,000, and imprisoned for not more than 6 months, or both, and shall be required to pay the costs of prosecution.

"(d) No patient record in the possession of an organization having a contract with the Secretary under this part shall be subject to subpena or discovery proceedings in a civil action.

"ANNUAL REPORTS

"Sec. 1161. The Secretary shall submit to the Congress not later than April 1 of each year, a full and complete report on the administration, impact, and cost of the program under this part during the preceding fiscal year, including data and information on—

"(1) the number, status, and service areas of all utilization and quality control peer review organizations participating in the program;

"(2) the number of health care institutions and practitioners whose services are subject to review by such organizations, and the number of beneficiaries and recipients who received services subject to such review during such year;

"(3) the various methods of reimbursement utilized in contracts under this part, and the relative efficiency of each such method of reimbursement;

"(4) the imposition of penalties and sanctions under this title for violations of law and for failure to comply with the obligations imposed by this part;

"(5) the total costs incurred under titles XVIII and XIX of this Act in the implementation and operation of all procedures required by such titles for the review of services to determine their medical necessity, appropriateness of use, and quality; and

"(6) descriptions of the criteria upon which decisions are made, and the selection and relative weights of such criteria.

"EXEMPTIONS OF CHRISTIAN SCIENCE SANATORIUMS

"SEC. 1162. The provisions of this part shall not apply with respect to a Christian Science sanatorium operated, or listed and certified, by the First Church of Christ, Scientist, Boston, Massachusetts.

"MEDICAL OFFICERS IN AMERICAN SAMOA, THE NORTHERN MARIANA ISLANDS, AND THE TRUST TERRITORY OF THE PACIFIC ISLANDS TO BE INCLUDED IN THE UTILIZATION AND QUALITY CONTROL PEER REVIEW PROGRAM

"SEC. 1163. For purposes of applying this part to American Samoa, the Northern Mariana Islands, and the Trust Territory of the Pacific Islands, individuals licensed to practice medicine in those places shall be considered to be physicians and doctors of medicine.".

FACILITATION OF PRIVATE REVIEW

SEC. 144. Section 1866(a)(1) of the Social Security Act is amended—

(1) by striking out "and" at the end of subparagraphs (A), (B), and (C);

(2) by striking out the period at the end of subparagraph (D) and inserting in lieu thereof ", and"; and

(3) by inserting after subparagraph (D) the following new subparagraph:

"(E) to release data with respect to patients of such provider upon request to an organization having a contract with the Secretary under part B of title XI as may be necessary (i) to allow such organization to carry out its functions under such contract, or (ii) to allow such organization to carry out similar review functions under any contract the organization may have with a private or public agency paying for health care in the same area with respect to patients who authorize release of such data for such purposes.".

WAIVER OF LIABILITY PROVISION

SEC. 145. Section 1879(a) of the Social Security Act is amended by adding at the end thereof the following new sentence: "Any provider or other person furnishing items or services for which payment may not be made by reason of section 1862(a)(1) or (9) shall be deemed to have knowledge that payment cannot be made for such items or services if the claim relating to such items or services involves a case, provider or other person furnishing services, procedure, or test, with respect to which such provider or other person has been notified by the Secretary (including notification by a utilization and quality control peer review organization) that a pattern of inappropriate utilization has occurred in the past, and such provider or other person has been allowed a reasonable time to correct such inappropriate utilization.".

MEDICAID PROVISIONS

SEC. 146. (a) Section 1902(d) of the Social Security Act is amended—

(1) by striking out "a Professional Standards Review Organization designated, conditionally or otherwise," and inserting in lieu thereof "a utilization and quality control peer review organization having a contract with the Secretary"; and

(2) by striking out "such Organization (or Organizations)" each place it appears and inserting in lieu thereof in each instance "such organization (or organizations)".

(b) Section 1903(a)(3)(C) of such Act is amended by striking out "Professional Standards Review Organization" and inserting in lieu thereof "utilization and quality control peer review organization".

DEMONSTRATION PROJECTS FOR COMPETITIVE BIDDING AND OTHER REIMBURSEMENT METHODS

SEC. 147. Section 402(a)(1) of the Social Security Amendments of 1967 (Public Law 90-248) is amended—

(1) by striking out "and" at the end of subparagraph (I);

(2) by striking out the period at the end of subparagraph (J) and inserting in lieu thereof "; and"; and

(3) by inserting after subparagraph (J) the following new subparagraph:

"(K) to determine whether the use of competitive bidding in the awarding of contracts, or the use of other methods of reimbursement, under part B of title XI would be efficient and effective methods of furthering the purposes of that part.".

TECHNICAL AMENDMENTS

SEC. 148. (a) Section 1862(d)(1)(C) of such Act is amended by striking out ", on the basis of reports transmitted to him in accordance with section 1157 of this Act (or, in the absence of any such report, on the basis of such data as he acquires in the administration of the program under this title)," and inserting in lieu thereof "on the basis of information acquired by the Secretary in the administration of this title".

(b) Sections 1815(b), 1861(v)(1)(G), and 1861(w)(2) of such Act are each amended by striking out "Professional Standards Review Organization" and inserting in lieu thereof in each instance "quality control and peer review organization".

(c) Section 1832(a)(2)(F)(ii) of such Act is amended by striking out "Professional Standards Review Organization (designated, conditionally or otherwise," and inserting in lieu thereof "quality control and peer review organization (having a contract with the Secretary".

(d) Section 1833(i) of such Act is amended by striking out "the National Professional Standards Review Council and".

(e) Section 1879(e) of such Act is amended by striking out "professional standards review organization" and inserting in lieu thereof "quality control and peer review organization".

EFFECTIVE DATE

SEC. 149. The amendments made by this part shall, subject to section 150, be effective with respect to contracts entered into or renewed on or after the date of the enactment of this Act.

MAINTENANCE OF CURRENT PSRO AGREEMENTS

SEC. 150. (a) The Secretary of Health and Human Services shall not terminate or fail to renew any agreement in effect with a professional standards review organization under part B of title XI of the Social Security Act on the earlier of the date of the enactment of this Act or September 30, 1982 until such time as he enters into a contract with a utilization and quality control peer review organization under such part, as amended by this subtitle, for the area served by such professional standards review organization. In complying with this subsection, the Secretary may renew any such contract with a professional standards review organization for a period of less than 12 months.

(b) The provisions of part B of title XI of the Social Security Act as in effect prior to the amendments made by this subtitle shall remain in effect with respect to contracts with professional standards review organizations in effect on the earlier of the date of the enactment of this Act or September 30, 1982, until such time as such contract is terminated or is not renewed, in accordance with subsection (a). Any matters awaiting a determination by a Statewide Professional Standards Review Council on the date of the enactment of this Act shall be transferred to the Secretary of Health and Human Services for a determination unless such determination is made by such Council within 30 days after the date of the enactment of this Act. No payments shall be made under part B of title XI of the Social Security Act to Statewide Professional Standards Review Councils for services performed under section 1162 of such Act after the end of such 30-day period.

SUBTITLE D—AID TO FAMILIES WITH DEPENDENT CHILDREN

ROUNDING OF ELIGIBILITY AND BENEFIT AMOUNTS

SEC. 151. (a) Section 402(a) of the Social Security Act is amended—

(1) by striking out "and" at the end of paragraph (32);

(2) by striking out the period at the end of paragraph (33) and inserting in lieu thereof "; and"; and

(3) by adding at the end thereof the following new paragraph:

"(34) provide that both the standard of need applied to a family and the amount of aid determined to be payable, when not a whole dollar amount, shall be rounded to the next lower whole dollar amount.".

(b) The amendment made by this section shall become effective on October 1, 1982.

EFFECTIVE DATE OF APPLICATION; PRORATION OF FIRST-MONTH'S AFDC BENEFIT

SEC. 152. (a) Section 402(a)(10) of the Social Security Act is amended—

(1) by striking out "provide, effective July 1, 1951, that all individuals" and inserting in lieu thereof "(A) provide that all individuals";

(2) by adding "and" after the semicolon; and

(3) by adding at the end thereof the following new subparagraph:

"(B) provide that an application for aid under the plan will be effective no earlier than the date such application is filed with the State agency or local agency responsible for the administration of the State plan, and the amount payable for the month in which the application becomes effective, if such application becomes effective after the first day of such month, shall bear the same ratio to the amount which would be payable if the application had been effective on the first day of such month as the number of days in the month including and following the effective date of the application bears to the total number of days in such month;".

(b) The amendments made by this section shall become effective on October 1, 1982.

ABSENCE FROM HOME SOLELY BY REASON OF UNIFORMED SERVICE

SEC. 153. (a) Section 406(a)(1) of the Social Security Act is amended by inserting "(other than absence occasioned solely by reason of the performance of active duty in the uniformed services of the United States)" "continued absence from the home".

(b) The amendment made by ths section shall become effective on October 1, 1982.

JOB SEARCH

SEC. 154. (a) Section 402(a) of the Social Security Act (as amended by section 151(a) of this Act) is further amended—

(1) by striking out "and" at the end of paragraph (33);

(2) by striking out the period at the end of paragraph (34) and inserting in lieu thereof "; and"; and

(3) by adding at the end thereof the following new paragraph:

"(35) at the option of the State, provide—

"(A) that as a condition of eligibility for aid under the State plan of any individual claiming such aid who is required to register pursuant to paragrpah (19)(A) (or who would be required to register under paragraph (19)(A) but for clause (iii) thereof), including all such individuals or only such groups, types, or classes thereof as the State agency may designate for purposes of this paragraph, such individual will be required to participate in a program of employment search—

"(i) beginning at the time he applies for such aid (or an application including his need is filed) and continuing for a period (prescribed by the State) of not more

than eight weeks (but this requirement may not be used as a reason for any delay in making a determination of an individual's eligibility for aid or in issuing a payment to or in behalf of any individual who is otherwise eligible for such aid); and

"(ii) at such time or times after the close of the period prescribed under clause (i) as the State agency may determine but not to exceed a total of 8 weeks in any 12 consecutive months;

"(B) that any individual participating in a program of employment search under this paragraph will be furnished such transportation and other services, or paid (in advance or by way of reimbursement) such amounts to cover transportation costs and other expenses reasonably incurred in meeting requirements imposed on him under this paragraph, as may be necessary to enable such individual to participate in such program; and

"(C) that, in the case of an individual who fails without good cause to comply with requirements imposed upon him under this paragraph, the sanctions imposed by paragraph (19)(F) shall be applied in the same manner as if the individual had made a refusal of the type which would cause the provisions of such paragraph (19)(F) to be applied (except that the State may at its option, for purposes of this paragraph, reduce the period for which such sanctions would otherwise be in effect).".

(b)(1) Section 403(a)(3)(C) of such Act is amended by inserting immediately after "expenditures" the following: "(including as expenditures under this subparagraph the value of any services furnished, and the amount of any payments made (to cover expenses incurred by individuals under a program of employment search), under section 402(a)(35)(B))".

(2) Section 403(a)(3) of such Act is further amended by striking out "other than services" in the matter immediately following subparagraph (C) and inserting in lieu thereof the following: "other than services furnished under section 402(a)(35)(B) (as described in the parenthetical phrase in subparagraph (C)), and other than services".

(c) Section 409(b)(3) of such Act is amended—

(1) in the first sentence—

(A) by inserting ", any program of employment search under section 402(a)(35)," after "pursuant to this section",

(B) by striking out "both such programs" and inserting in lieu thereof "more than one such program", and

(C) by striking out "in the other" and inserting in lieu thereof "in another"; and

(2) in the second sentence, by striking out "both such programs" and inserting in lieu thereof "more than one such program".

(d) The amendments made by this section shall become effective on October 1, 1982.

PRORATION OF STANDARD AMOUNT FOR SHELTER AND UTILITIES

SEC. 155. (a) Section 412 of the Social Security Act is amended to read as follows:

"PRORATING SHELTER ALLOWANCE OF AFDC FAMILY LIVING WITH ANOTHER HOUSEHOLD

"SEC. 412. A State plan for aid and services to needy families with children may provide that, in determining the need of any dependent child or relative claiming aid who is living with other individuals (not claiming aid together with such child or relative) as a household (as defined, for purposes of this section, by the Secretary), the amount included in the standard of need, and the payment standard, applied to such child or relative for shelter, utilities, and similar needs may be prorated on a reasonable basis, in such manner and under such circumstances as the State may determine to be appropriate. For purposes of any method of proration used by a State under this section, there shall not be included as a member of a household an individual receiving benefits under title XVI in any month to whom the one-third reduction prescribed by section 1612(a)(2)(A)(i) is applied.".

(b) The amendment made by this section shall become effective on October 1, 1982.

LIMITATION ON FEDERAL FINANCIAL PARTICIPATION IN ERRONEOUS ASSISTANCE EXPENDITURES

SEC. 156. (a) Section 403(i) of the Social Security Act is amended to read as follows:

"(i)(1)(A) Notwithstanding subsection (a)(1), if the ratio of a State's erroneous excess payments (as defined in subparagraph (C)) to its total payments under the State plan, approved under this part exceeds—

"(i) 0.04 for fiscal year 1983, or

"(ii) 0.03 for any fiscal year thereafter,

then the Secretary shall make no payment for such fiscal year with respect to so much of the erroneous excess payments (as so defined) as exceeds the allowable error rate for such fiscal year.

"(B) The Secretary may waive, in certain limited cases, all or part of the reduction required under subparagraph (A) with respect to any State if such State is unable to reach the allowable error rate for a fiscal year despite a good faith effort by such State.

"(C) For purposes of this subsection, the term 'erroneous excess payments' means that total of (i) payments to ineligible families, and (ii) overpayments to eligible families.

"(2) The State agency administering the plan approved under this part shall, at such times and in such form as the Secretary may specify, provide information on the rates of erroneous excess payments made in connection with its administration of such plan, together with any other data he requests that are reasonably necessary for him to carry out the provisions of this subsection.

"(3)(A) If a State fails to cooperate with the Secretary in providing information necessary to carry out this subsection, the Secretary, directly or through contractual or such other arrangements as he may

find appropriate, shall establish the error rates for that State on the basis of the best data reasonably available to him and in accordance with such techniques for sampling and estimating as he finds appropriate.

"(B) In any case in which it is necessary for the Secretary to exercise his authority under subparagraph (A) to determine a State's error rate for a fiscal year, the amount that would otherwise be payable to such State under this part for quarters in such year shall be reduced by the costs incurred by the Secretary in making (directly or otherwise) such determination.

"(4) This subsection shall not apply with respect to Puerto Rico, Guam, or the Virgin Islands.".

(b) Section 403(a) of such Act is amended by striking out "In the case of calendar quarters beginning after September 30, 1977, and prior to April 1, 1978, the amount to be paid to each State (as determined under the preceding provisions of this subsection or section 1118, as the case may be) shall be increased in accordance with the provisions of subsection (i) of this section.".

(c) Section 403(j) of such Act is amended by striking out "If the dollar error rate of aid furnished by a State" and inserting in lieu thereof "In the case of Puerto Rico, Guam, or the Virgin Islands, if the dollar error rate of aid furnished by such State".

(d)(1) The amendments made by subsections (a) and (b) shall become effective on October 1, 1982.

(2) The inapplicability of section 403(j) of the Social Security Act to States other than Puerto Rico, Guam, and the Virgin Islands by reason of the amendment made by subsection (c) shall be effective with respect to six-month periods beginning after April 1983.

(e) The regulations currently in effect for fiscal year 1982 with respect to erroneous payments made by States under a State plan approved under part A of title IV of the Social Security Act (45 CFR 205.42) shall remain in effect with respect to erroneous payments made by States until new regulations reflecting the changes made by subsection (a) are promulgated and placed in effect.

EXCLUSION FROM INCOME OF CERTAIN STATE PAYMENTS

SEC. 157. (a) The last sentence of section 403(a) of the Social Security Act is amended by inserting before the period at the end thereof the following: ", but any such amount, if determined to have been paid by the State in recognition of the difference between the current or anticipated needs of a family for a month based upon actual income or other relevant circumstances for such month, and the needs of such family for such month based upon income and other relevant circumstances as retrospectively determined under section 402(a)(13)(A)(ii), shall not be considered income within the meaning of section 402(a)(13) for the purpose of determining the amount of aid in the succeeding months".

(b) The amendment made by this section shall become effective on October 1, 1982.

EXTENSION OF TIME FOR STATES TO ESTABLISH A WORK INCENTIVE DEMONSTRATION PROGRAM

SEC. 158. (a) Section 445(b)(1) of the Social Security Act is amended by striking out "Not later than sixty days following the date of the enactment of this section" and inserting in lieu thereof "Not later than June 30, 1984".

(b) Section 445(b)(1)(B) of such Act is amended by inserting before the semicolon at the end thereof the following: ", but subject to waiver of such criteria as provided under section 1115".

(c) The amendments made by this section shall become effective on the date of the enactment of this Act.

EXCLUSION FROM INCOME

SEC. 159. Notwithstanding any other provision of law, payments which are made, under a statutorily established State program, to meet certain needs of children receiving aid under the State's plan approved under part A of title IV of the Social Security Act, if—

(1) the payments are made to such children by the State agency administering such plan, but are made without Federal financial participation (under section 403(a) of such Act or otherwise), and

(2) the State program has been continuously in effect since before January 1, 1979,

shall be excluded from the imcome of such children and their families for purposes of section 402(a)(17) of such Act, and for all the other purposes of such part A and of such plan, effective on the date of the enactment of this Act.

TECHNICAL AMENDMENTS TO SOCIAL SERVICES AND FOSTER CARE PROVISIONS IN 1981 RECONCILIATION ACT

SEC. 160. (a) Section 1108(a) of the Social Security Act is amended by adding at the end thereof after and below paragraph (3)(F))

"Each jurisdiction specified in this subsection may use in its program under title XX any sums available to it under this subsection which are not needed to carry out the programs specified in this subsection."

(b) Section 2003(b) of such Act is amended in the matter following clause (2) by inserting "(other than Puerto Rico, Guam, the Virgin Islands, and the Northern Mariana Islands)" after "the population of all States".

(c) The last sentence of section 1101(a)(1) of such Act is amended by striking out "American Samoa, the Northern Mariana Islands, and the Trust Territory of the Pacific Islands" and inserting in lieu thereof "Guam, and the Northern Mariana Islands".

(d) Section 2353(r) of the Omnibus Budget Reconciliation Act of 1981 is amended to read as follows:

"(r) Section 471(a)(10) of such Act is amended to read as follows:

"'(10) provides for the establishment or designation of a State authority or authorities which shall be responsible for establishing and maintaining standards for foster family homes and child care institutions which are reasonably in accord with recommended standards of national organizations concerned with

standards for such institutions or homes, including standards related to admission policies, safety, sanitation, and protection of civil rights, and provides that the standards so established shall be applied by the State to any foster family home or child care institution receiving funds under this part or part B of this title;'."

(e) The amendments made by this section shall be effective as of October 1, 1981.

DELAYED EFFECTIVE DATE IN CASES REQUIRING CONFORMING STATE LEGISLATION

SEC. 161. In the case of a State with respect to which the Secretary of Health and Human Services has determined that State legislation is required in order to conform the State plan approved under part A of title IV of the Social Security Act to the requirements imposed by an amendment made by this subtitle, the State plan shall not be regarded as failing to comply with the requirements of such part solely by reason of its failure to meet the requirements imposed by such amendment prior to the end of the first session of the State legislature which begins after October 1, 1982, or which began prior to October 1, 1982, and remained in session for at least twenty-five calendar days after such date. For purposes of the preceding sentence, the term "session" means a regular, special, budget, or other session of a State legislature.

Subtitle E—Child Support Enforcement

FEE FOR SERVICES TO NON-AFDC FAMILIES

SEC. 171. (a) Section 454(6) of the Social Security Act is amended—

(1) in clause (A), by inserting "including, at the option of the State, support collection services for the spouse (or former spouse) with whom the absent parent's child is living (but only if a support obligation has been established with respect to such spouse)," after "with the State,";

(2) in clause (B), by striking out "services under the State plan (other than collection of support)" and inserting in lieu thereof "such services"; and

(3) by amending clause (C) to read as follows: "(C) any costs in excess of the fee so imposed may be collected—

"(i) from the parent who owes the child or spousal support obligation involved, or

"(ii) at the option of the State, from the individual to whom such services are made available, but only if such State has in effect a procedure whereby all persons in such State having authority to order child or spousal support are informed that such costs are to be collected from the individual to whom such services were made available;"

(b)(1) Section 454 of such Act is further amended—

(A) by adding "and" after the semicolon at the end of paragraph (18);

(B) by striking out paragraph (19); and

(C) by redesignating paragraph (20) as paragraph (19).

(2) Section 2333(c) of the Omnibus Budget Reconciliation Act of 1981 is amended by striking out "Section 453(a) of such Act is amended" and inserting in lieu thereof "Section 455(a) of such Act is amended".

(3) Section 303(e)(2)(A)(iii)(II) of the Social Security Act is amended by striking out "454(20)(B)(i)" and inserting in lieu thereof "454(19)(B)(i)".

(c) The amendments made by this section shall be effective on and after August 13, 1981.

ALLOTMENTS FROM PAY FOR CHILD AND SPOUSAL SUPPORT OWED BY MEMBERS OF THE UNIFORMED SERVICES ON ACTIVE DUTY

SEC. 172.(a) Part D of title IV of the Social Security Act is amended by adding at the end thereof the following new section:

"ALLOTMENTS FROM PAY FOR CHILD AND SPOUSAL SUPPORT OWED BY MEMBERS OF THE UNIFORMED SERVICES ON ACTIVE DUTY

"SEC. 465. (a)(1) In any case in which child support payments or child and spousal support payments are owed by a member of one of the uniformed services (as defined in section 101(3) of title 37, United States Code) on active duty, such member shall be required to make allotments from his pay and allowances (under chapter 13 of title 37, United States Code) as payment of such support, when he has failed to make periodic payments under a support order that meets the criteria specified in section 303(b)(1)(A) of the Consumer Credit Protection Act (15 U.S.C. 1673(b)(1)(A)) and the resulting delinquency in such payments is in a total amount equal to the support payable for two months or longer. Failure to make such payments shall be established by notice from an authorized person (as defined in subsection (b)) to the designated official in the appropriate uniformed service. Such notice (which shall in turn be given to the affected member) shall also specify the person to whom the allotment is to be payable. The amount of the allotment shall be the amount necessary to comply with the order (which, if the order so provides, may include arrearages as well as amounts for current support), except that the amount of the allotment, together with any other amounts withheld for support from the wages of the member, as a percentage of his pay from the uniformed service, shall not exceed the limits prescribed in sections 303 (b) and (c) of the Consumer Credit Protection Act (15 U.S.C. 1673 (b) and (c)). An allotment under this subsection shall be adjusted or discontinued upon notice from the authorized person.

"(2) Notwithstanding the preceding provisions of this subsection, no action shall be taken to require an allotment from the pay and allowances of any member of one of the uniformed services under such provisions (A) until such member has had a consultation with a judge advocate of the service involved (as defined in section 801(13) of title 10, United States Code), or with a law specialist (as defined in section 801(11) of such title) in the case of the Coast Guard, or with a legal officer designated by the Secretary concerned (as defined in section 101(5) of title 37, United States code) in any other case, in person, to discuss the legal and other factors involved

with respect to the member's support obligation and his failure to make payments thereon, or (B) until 30 days have elapsed after the notice described in the second sentence of paragraph (1) is given to the affected member in any case where it has not been possible, despite continuing good faith efforts, to arrange such a consultation.

"(b) For purposes of this section the term 'authorized person' with respect to any member of the uniformed services means—

"(1) any agent or attorney of a State having in effect a plan approved under this part who has the duty or authority under such plan to seek to recover any amounts owed by such member as child or child and spousal support (including, when authorized under the State plan, any official of a political subdivision); and

"(2) the court which has authority to issue an order against such member for the support and maintenance of a child, or any agent of such court.

"(c) The Secretary of Defense, in the case of the Army, Navy, Air Force, and Marine Corps, and the Secretary concerned (as defined in section 101(5) of title 37, United States Code) in the case of each of the other uniformed services, shall each issue regulations applicable to allotments to be made under this section, designating the officials to whom notice of failure to make support payments, or notice to discontinue or adjust an allotment, should be given, prescribing the form and content of the notice and specifying any other rules necessary for such Secretary to implement this section.".

(b) The amendment made by subsection (a) shall become effective on October 1, 1982.

REIMBURSEMENT OF STATE AGENCY IN INITIAL MONTH OF INELIGIBILITY FOR AFDC

SEC. 173. (a) Section 454(5) of the Social Security Act is amended by inserting "following the first month" after "for any month".

(b) The amendment made by this section shall become effective on October 1, 1982.

REDUCTION IN CERTAIN FEDERAL PAYMENTS TO STATES UNDER CHILD SUPPORT ENFORCEMENT PROGRAM

SEC. 174. (a) Section 455(a)(1) of the Social Security Act is amended by striking out "75 percent" and inserting in lieu thereof "70 percent".

(b) Section 455(c) of such Act is repealed.

(c) Section 458(a) of such Act is amended by striking out "15 per centum" and inserting in lieu thereof "12 percent".

(d) The amendment made by subsection (a) shall apply with respect to quarters beginning on or after October 1, 1982. Subsection (b) shall apply with respect to quarters beginning on or after October 1, 1983; and the amendment made by subsection (c) shall apply with respect to amounts collected on or after October 1, 1983.

TECHNICAL AMENDMENTS TO CHILD SUPPORT ENFORCEMENT PROVISIONS IN RECONCILIATION ACT

SEC. 175. (a)(1) The first sentence of section 452(b) of the Social Security Act is amended by striking out "certify" and all that follows and inserting in lieu thereof "certify to the Secretary of the Treasury for collection pursuant to the provisions of section 6305 of the Internal Revenue Code of 1954 the amount of any child support obligation (including any support obligation with respect to the parent who is living with the child and receiving aid under the State plan approved under part A) which is assigned to such State or is undertaken to be collected by such State pursuant to section 454(6)."

(2) Section 303(e)(2)(A)(i) of such Act is amended by striking out "of this subsection" and inserting in lieu thereof "of paragraph (1)".

(b) The amendments made by this section shall be effective as of October 1, 1981.

DELAYED EFFECTIVE DATE IN CASES REQUIRING STATE LEGISLATION

SEC. 176. In the case of a State with respect to which the Secretary of Health and Human Services has determined that State legislation is required in order to conform the State plan approved under part D of title IV of the Social Security Act to the requirements imposed by any amendment made by this subtitle, the State plan shall not be regarded as failing to comply with the requirements of such part solely by reason of its failure to meet the requirements imposed by such amendment prior to the end of the first session of the State legislature which begins after October 1, 1982, or which began prior to October 1, 1982, and remained in session for at least twenty-five calendar days after such date. For purposes of the preceding sentence, the term "session" means a regular, special, budget, or other session of a State legislature.

Subtitle F—Supplemental Security Income

EFFECTIVE DATE OF APPLICATION; PRORATION OF INITIAL SSI BENEFIT PAYMENT

SEC. 181. (a) Section 1611(c) of the Social Security Act is amended by striking out paragraphs (2) and (3) and inserting in lieu thereof the following new paragraphs:

"(2) The amount of such benefit for the month in which an application for benefits becomes effective (or, if the Secretary so determines, for such month and the following month) and for any month immediately following a month of ineligibility for such benefits (or, if the Secretary so determines, for such month and the following month) shall—

> *"(A) be determined on the basis of the income of the individual and the eligible spouse, if any, of such individual and other relevant circumstances in such month; and*
>
> *"(B) in the case of the month in which an application becomes effective or the first month following a period of ineligi-*

bility, if such application becomes effective, or eligibility is restored, after the first day of such month, bear the same ratio to the amount of the benefit which would have been payable to such individual if such application had become effective, or eligibility had been restored, on the first day of such month as the number of days in such month including and following the effective date of such application or restoration of eligibility bears to the total number of days in such month.

"(3) For purposes of this subsection, an application of an individual for benefits under this title shall be effective on the later of—

"(A) the date such application is filed, or

"(B) the date such individual first becomes eligible for such benefits with respect to such application.".

(b) The amendment made by this section shall become effective on October 1, 1982.

ROUNDING OF SSI ELIGIBILITY AND BENEFIT AMOUNTS

SEC. 1821. (a) Section 1617 of the Social Security Act is amended to read as follows:

"COST-OF-LIVING ADJUSTMENTS IN BENEFITS

"SEC. 1617. (a) Whenever benefit amounts under title II are increased by any percentage effective with any month as a result of a determination made under section 215(i)—

"(1) each of the dollar amounts in effect for such month under subsections (a)(1)(A), (a)(2)(A), (b)(1), and (b)(2) of section 1611, and subsection (a)(1)(A) of section 211 of Public Law 93-66, as specified in such subsections or as previously increased under this section, shall be increased by the amount (if any) by which—

"(A) the amount which would have been in effect for such month under such subsection but for the rounding of such amount pursuant to paragraph (2), exceeds

"(B) the amount in effect for such month under such subsection; and

"(2) the amount obtained under paragraph (1) with respect to each subsection shall be further increased by the same percentage by which benefit amounts under title II are increased for such month (and rounded, when not a multiple of $12, to the next lower multiple of $12), effective with respect to benefits for months after such month.

"(b) The new dollar amounts to be in effect under section 1611 of this title and under section 211 of Public Law 93-66 by reason of this section shall be published in the Federal Register together with, and at the same time as, the material required by section 215(i)(2)(D) to be published therein by reason of the determination involved.".

(b) The amendment made by this section shall become effective on October 1, 1982.

COORDINATION OF SSI AND OASDI COST-OF-LIVING ADJUSTMENTS

SEC. 183. (a) Section 1611(c) of the Social Security Act (as amended by section 181 of this Act) is further amended--

(1) in paragraph (1) by striking out "paragraph (2)" and inserting in lieu thereof "paragraphs (2), (3), and (4)";

(2) by redesignating paragraphs (3) and (4) as paragraphs (5) and (6), respectively; and

(3) by inserting after paragraph (2) the following new paragraphs:

"(3) For purposes of this subsection, an increase in the benefit amount payable under title II (over the amount payable in the preceding month, or, at the election of the Secretary, the second preceding month) to an individual receiving benefits under this title shall be included in the income used to determine the benefit under this title of such individual for any month which is–

"(A) the first month in which the benefit amount payable to such individual under this title is increased pursuant to section 1617, or

"(B) at the election of the Secretary, the month immediately following such month.

"(4)(A) Notwithstanding paragraph (3), if the Secretary determines that reliable information is currently available with respect to the income and other circumstances of an individual for a month (including information with respect to a class of which such individual is a member and information with respect to scheduled cost-of-living adjustments under other benefit programs), the benefit amount of such individual under this title for such month may be determined on the basis of such information.

"(B) The Secretary shall prescribe by regulation the circumstances in which information with respect to an event may be taken into account pursuant to subparagraph (A) in determining benefit amounts under this title.".

(b) The amendment made by subsection (a) shall become effective October 1, 1982.

PHASEOUT OF HOLD HARMLESS PROTECTION

SEC. 184. (a) Section 401 of the Social Security Amendments of 1972 (Public Law 92-603) is amended by adding at the end thereof the following new subsection:

"(d) In addition to the amount which a State must pay to the Secretary for the fiscal year 1983 or the fiscal year 1984, as determined under subsection (a), the State shall also pay, for the fiscal year 1983, 60 percent of the further amount that would be payable but for the limit specified in subsection (a), and, for the fiscal year 1984, 80 percent of such further amount. For each fiscal year thereafter, the limit prescribed in subsection (a) shall be inapplicable and a State shall pay to the Secretary the full amount of any supplementary payments he makes on behalf of such State.".

(b) The amendment made by subsection (a) shall become effective on the date of the enactment of this Act.

EXCLUSION FROM RESOURCES OF BURIAL PLOTS AND CERTAIN FUNDS SET ASIDE FOR BURIAL EXPENSES

SEC. 185. (a) Section 1613(a)(2) of the Social Security Act is amended by inserting "(A)" after "(2)", by adding "and' after the semicolon, and by adding at the end thereof the following new subparagraph:

> *"(B) the value of any burial space (subject to such limits as to size or value as the Secretary may by regulation prescribe) held for the purpose of providing a place for the burial of the individual, his spouse, or any other member of his immediate family;".*

(b) Section 1613 of such Act is further amended by adding at the end thereof the following new subsection:

"FUNDS SET ASIDE FOR BURIAL EXPENSES

"(d)(1) In determining the resources of an individual, there shall be excluded an amount, not in excess of $1,500 each with respect to such individual and his spouse (if any), that is separately identifiable and has been set aside to meet the burial and related expenses of such individual or spouse if the inclusion of any portion of such amount or amounts would cause the resources of such individual, or of such individual and spouse, to exceed the limits specified in paragraph (1) or (2) (whichever may be applicable) of section 1611(a).

"(2) The amount of $1,500, referred to in paragraph (1), with respect to an individual shall be reduced by an amount equal to (A) the total face value of all insurance policies on his life which are owned by him or his spouse and the cash surrender value of which has been excluded in determining the resources of such individual or of such individual and his spouse, and (B) the total of any amounts in an irrevocable trust (or other irrevocable arrangement) available to meet the burial and related expenses of such indiviudal or his spouse.

"(3) If the Secretary finds that any part of the amount excluded under paragraph (1) was used for purposes other than those for which it was set aside, he shall reduce any future benefits payable to the eligible individual (or to such individual and his spouse) by an amount equal to such part.

"(4) The Secretary may provide by regulations that whenever an amount set aside to meet burial and related expenses is excluded under paragraph (1) in determining the resources of an individual, any interest earned or accrued on such amount (and left to accumulate), and any appreciation in the value of prepaid burial arrangements for which such amount was set aside, shall also be excluded (to such extent and subject to such conditions or limitations as such regulations may prescribe) in determining the resources (and the income) of such individual.".

(c) The amendment made by this section shall take effect on the first day of the second month after the month in which this Act is enacted.

MANDATORY PASSTHROUGH UNDER STATE SUPPLEMENTATION PROVISIONS

SEC. 186. Section 1618 of the Social Security Act is amended by adding at the end thereof the following new subsection:

"(c) Any State which satisfies the requirements of this section solely by reason of subsection (b) for a particular month or months in any 12-month period (described in such subsection) ending on or after June 30, 1982, may elect, with respect to any month in any subsequent 12-month period (so described), to apply subsection (a)(4) as though the reference to December 1976 in such subsection were a reference to the month of December which occurred in the 12-month period immediately preceding such subsequent period.".

TREATMENT OF UNNEGOTIATED CHECKS UNDER SUPPLEMENTAL SECURITY INCOME PROGRAM.

SEC. 187. (a) Section 1631(i)(2) of the Social Security Act (as added by section 2343(a) of the Omnibus Budget Reconciliation Act of 1981) is amended by striking out "included in all checks payable to individuals entitled to benefits under this title but" in the first sentence and inserting in lieu thereof "included in all such benefit checks".

(b) The amendment made by subsection (a) shall become effective October 1, 1982.

SUBTITLE G—UNEMPLOYMENT COMPENSATION

ROUNDING OF BENEFIT AMOUNTS

SEC. 191. (a) Section 204(a)(2) of the Federal-State Extended Unemployment Compensation Act of 1970 is amended by striking out "or" at the end of clause (B), and by inserting before the period at the end thereof the following: ", or (D) paid to an individual with respect to a week of unemployment to the extent that such amount exceeds the amount of such compensation which would be paid to such individual if such State had a benefit structure which provided that the amount of compensation otherwise payable to any individual for any week shall be rounded (if not a full dollar amount) to the nearest lower full dollar amount".

(b)(1) Except as provided in paragraph (2), the amendments made by this section shall apply in the case of compensation paid to individuals during eligibility periods beginning on or after October 1, 1983.

(2) In the case of a State with respect to which the Secretary of Labor has determined that State legislation is required in order to provide for rounding down of unemployment compensation amounts, the amendment made by this section shall apply in the case of compensation paid to individuals during eligibility periods which begin on or after October 1, 1983, and after the end of the first session of the State legislature which begins after the date of the enactment of this Act, or which began prior to the date of the enactment of this Act and remained in session for at least twenty-five calendar days after such date of enactment. For purposes of the

preceding sentence, the term "session" means a regular, special, budget, or other session of a State legislature.

USE OF CERTAIN AMOUNTS TRANSFERRED TO STATE UNEMPLOYMENT FUNDS

SEC. 192. (a) Paragraph (2) of section 903(c) of the Social Security Act is amended—

(1) by striking out "twenty-four" each place it appears and inserting in lieu thereof "thirty-four"; and

(2) by striking out "twenty-fourth" in the second sentence and inserting in lieu thereof "thirty-fourth".

(b) Subsection (c) of section 903 of such Act is amended by adding at the end thereof the following new paragraph:

"(3)(A) If—

"(i) amounts transferred to the account of a State pursuant to subsections (a) and (b) of this section were used in payment of unemployment benefits to individuals; and

"(ii) the Governor of such State submits a request to the Secretary of Labor that such amounts be restored under this paragraph,

then the amounts described in clause (i) shall be restored to the status of funds transferred under subsections (a) and (b) of this section which have not been used by eliminating any charge against amounts so transferred for the use of such amounts in the payment of unemployment benefits.

"(B) Subparagraph (A) shall apply only to the extent that the amounts described in clause (i) of such subparagraph do not exceed the amount then in the State's account.

"(C) Subparagraph (A) shall not apply if the State has a balance of advances made to its account under title XII of this Act.

"(D) If the Secretary of Labor determines that the requirements of this paragraph are met with respect to any request, the Secretary shall notify the Governor of the State that such requirements are met with respect to such request and the amount restored under this paragraph. Such restoration shall be as of the first day of the first month following the month in which the notification is made.".

TREATMENT OF CERTAIN EMPLOYEES OF INSTITUTIONS OF HIGHER EDUCATION

SEC. 193. (a) Clause (ii) of section 3304(a)(6)(A) of the Internal Revenue Code of 1954 (relating to requirements for approval of State unemployment compensation laws) is amended to read as follows:

"(ii) with respect to services in any other capacity for an educational institution to which section 3309(a)(1) applies—

"(I) compensation payable on the basis of such services may be denied to any individual for any week which commences during a period between 2 successive academic years or terms if such individual performs such services in the first of such academic years or terms and there is a reasonable assurance that such individual will perform such services in the second of such academic years or terms, except that

"(II) if compensation is denied to any individual for any week under subclause (I) and such individual was not offered an opportunity to perform such services for the educational institution for the second of such academic years or terms, such individual shall be entitled to a retroactive payment of the compensation for each week for which the individual filed a timely claim for compensation and for which compensation was denied solely by reason of subclause (I),".

(b)(1) The amendment made by subsection (a) shall apply to weeks of unemployment beginning after the date of the enactment of this Act.

(2) The amendment made by subsection (a), insofar as it requires retroactive payments of compensation to employees of educational institutions other than institutions of higher education (as defined in section 3304(f) of the Internal Revenue Code of 1954), shall not be a requirement for any State law before January 1, 1984.

SHORT-TIME COMPENSATION

SEC. *194. (a) It is the purpose of this section to assist States which provide partial unemployment benefits to individuals whose workweeks are reduced pursuant to an employer plan under which such reductions are made in lieu of temporary layoffs.*

(b)(1) The Secretary of Labor (hereinafter in this section referred to as the "Secretary") shall develop model legislative language which may be used by States in developing and enacting short-time compensation programs, and shall provide technical assistance to States to assist in developing, enacting, and implementing such short-time compensation program.

(2) The Secretary shall conduct a study or studies for purposes of evaluating the operation, costs, effect on the State insured rate of unemployment, and other effects of State short-time compensation programs developed pursuant to this section.

(3) This section shall be a three-year experimental provision, and the provisions of this section regarding guidelines shall terminate 3 years following the date of the enactment of this Act.

(4) States are encouraged to experiment in carrying out the purpose and intent of this section. However, to assure minimum uniformity, States are encouraged to consider requiring the provisions contained in subsections (c) and (d).

(c) For purposes of this section, the term "short-time compensation program" means a program under which—

(1) individuals whose workweeks have been reduced pursuant to a qualified employer plan by at least 10 per centum will be eligible for unemployment compensation;

(2) the amount of unemployment compensation payable to any such individual shall be a pro rata portion of the unemployment compensation which would be payable to the individual if the individual were totally unemployed;

(3) eligible employees may be eligible for short-time compensation or regular unemployment compensation, as needed; except that no employee shall be eligible for more than the maximum entitlement during any benefit year to which he or she would

have been entitled for total unemployment, and no employee shall be eligible for short-time compensation for more than twenty-six weeks in any twelve-month period; and

(4) eligible employees will not be expected to meet the availability for work or work search test requirements while collecting short-time compensation benefits, but shall be available for their normal workweek.

(d) For purposes of subsection (c), the term "qualified employer plan" means a plan of an employer or of an employers' association which association is party to a collective bargaining agreement (hereinafter referred to as "employers' association") under which there is a reduction in the number of hours worked by employees rather than temporary layoffs if—

(1) the employer's or employers' association's short-time compensation plan is approved by the State agency;

(2) the employer or employers' association certifies to the State agency that the aggregate reduction in work hours pursuant to such plan is in lieu of temporary layoffs which would have affected at least 10 per centum of the employees in the unit or units to which the plan would apply and which would have resulted in an equivalent reduction of work hours;

(3) during the previous four months the work force in the affected unit or units has not been reduced by temporary layoffs of more than 10 per centum;

(4) the employer continues to provide health benefits, and retirement benefits under defined benefit pension plans (as defined in section 3(35) of the Employee Retirement Income Security Act of 1974, to employees whose workweek is reduced under such plan as though their workweek had not been reduced; and

(5) in the case of employees represented by an exclusive bargaining representative, that representative has consented to the plan.

The State agency shall review at least annually any qualified employer plan put into effect to assure that it continues to meet the requirements of this subsection and of any applicable State law.

(e) Short-time compensation shall be charged in a manner consistent with the State law.

(f) For purposes of this section, the term "State" includes the District of Columbia, the Commonwealth of Puerto Rico, and the Virgin Islands.

(g)(1) The Secretary shall conduct a study or studies of State short-time compensation programs consulting with employee and employer representatives in developing criteria and guidelines to measure the following factors:

(A) the impact of the program upon the unemployment trust fund, and a comparison with the estimated impact on the fund of layoffs which would have occurred but for the existence of the program;

(B) the extent to which the program has protected and preserved the jobs of workers, with special emphasis on newly hired employees, minorities, and women;

(C) the extent to which layoffs occur in the unit subsequent to initiation of the program and the impact of the program upon

the entitlement to unemployment compensation of the employees;

(D) where feasible, the effect of varying methods of administration;

(E) the effect of short-time compensation on employers' State unemployment tax rates, including both users and nonusers of short-time compensation, on a State-by-State basis;

(F) the effect of various State laws and practices under those laws on the retirement and health benefits of employees who are on short-time compensation programs;

(G) a comparison of costs and benefits to employees, employers, and communities from use of short-time compensation and layoffs;

(H) the cost of administration of the short-time compensation program; and

(I) such other factors as may be appropriate.

(2) Not later than October 1, 1985, the Secretary shall submit to the Congress and to the President a final report on the implementation of this section. Such report shall contain an evaluation of short-time compensation programs and shall contain such recommendations as the Secretary deems advisable, including recommendations as to necessary changes in the statistical practices of the Department of Labor.

TITLE II—REVENUE MEASURES

Subtitle A—Provisions Relating to Individuals

SEC. 201. ALTERNATIVE MINIMUM TAX ON TAXPAYERS OTHER THAN CORPORATIONS.

(a) IN GENERAL.—Section 55 (relating to alternative minimum tax for taxpayers other than corporations) is amended to read as follows:

"SEC. 55. ALTERNATIVE MINIMUM TAX FOR TAXPAYERS OTHER THAN CORPORATIONS.

"(a) TAX IMPOSED.—In the case of a taxpayer other than a corporation, there is imposed (in addition to any other tax imposed by this subtitle) a tax equal to the excess (if any) of—

"(1) an amount equal to 20 percent of so much of the alternative minimum taxable income as exceeds the exemption amount, over

"(2) the regular tax for the taxable year.

"(b) ALTERNATIVE MINIMUM TAXABLE INCOME.—For purposes of this title, the term 'alternative minimum taxable income' means the adjusted gross income (determined without regard to the deduction allowed by section 172) of the taxpayer for the taxable year—

"(1) reduced by the sum of—

"(A) the alternative tax net operating loss deduction, plus

"(B) the alternative tax itemized deductions, plus

"(C) any amount included in income under section 667, and

"(2) increased by the amount of items of tax preference.

"(c) Credits.—

"(1) In general.—For purposes of determining any credit allowable under subpart A of part IV of this subchapter (other than the foreign tax credit allowed under section 33(a))—

"(A) the tax imposed by this section shall not be treated as a tax imposed by this chapter, and

"(B) the amount of the foreign tax credit allowed by section 33(a) shall be determined without regard to this section.

"(2) Foreign tax credit allowed against alternative minimum tax.—

"(A) Determination of foreign tax credit.—The total amount of the foreign tax credit which can be taken against the tax imposed by subsection (a) shall be determined under subpart A of part III of subchapter N (section 901 and following).

"(B) Increase in amount of foreign taxes taken into account.—For purposes of the determination provided by subparagraph (A), the amount of the taxes paid or accrued to foreign countries or possessions of the United States during the taxable year shall be increased by an amount equal to the lesser of—

"(i) the foreign tax credit allowable under section 33(a) in computing the regular tax for the taxable year, or

"(ii) the tax imposed by subsection (a).

"(C) Section 904(a) limitation.—For purposes of the determination provided by subparagraph (A), the limitation of section 904(a) shall be an amount equal to the same proportion of the sum of the tax imposed by subsection (a) against which such credit is taken and the regular tax as—

"(i) the taxpayer's alternative minimum taxable income from sources without the United States (but not in excess of the taxpayer's entire alternative minimum taxable income), bears to

"(ii) his entire alternative minimum taxable income.

For such purpose, the amount of the limitation of section 904(a) shall not exceed the tax imposed by subsection (a).

"(D) Definition of alternative minimum taxable income from sources without the United States.—For purposes of subparagraph (C), the term 'alternative minimum taxable income from sources without the United States' means adjusted gross income from sources without the United States, adjusted as provided in paragraphs (1) and (2) of subsection (b) (taking into account in such adjustment only items described in such paragraphs which are properly attributable to items of gross income from sources without the United States).

"(E) Special rule for applying section 904(c).—In determining the amount of foreign taxes paid or accrued during the taxable year which may be deemed to be paid or accrued in a preceding or succeeding taxable year under section 904(c)—

"(i) the limitation of section 904(a) shall be increased by the amount of the limitation determined under subparagraph (C), and

"(ii) any increase under subparagraph (B) shall be taken into account.

"(3) Carryover and carryback of certain credits.—

"(A) In general.—In the case of any taxable year in which a tax is imposed by this section, for purposes of determining the amount of any carryback or carryover of any applicable credit to any other taxable year, the amount of the applicable credit limitation for such taxable year shall be deemed to be—

"(i) the amount of the applicable credit allowable for such taxable year (determined without regard to this paragraph), reduced (but not below zero) by

"(ii) the amount of the tax imposed by this section for the taxable year, reduced by—

"(I) the amount of the credit allowable under section 33(a), and

"(II) the amount of such tax taken into account under this clause with respect to any applicable credit having a lower number or letter designation.

"(B) Applicable credits, etc.—For purposes of this paragraph—

"(i) Applicable credit.—The term 'applicable credit' means any credit allowable under section 38, 40, 44B, 44C, 44E, or 44F.

"(ii) Applicable credit limitation.—The term 'applicable credit limitation' means, with respect to any applicable credit, the limitation under section 46(a)(3), 53(a), 44C(b)(5), 44E(e)(1), 44F(g)(1), or 50A(a)(2), whichever is appropriate.

"(d) Alternative Tax Net Operating Loss Deduction Defined.—For purposes of this section—

"(1) In general.—The term 'alternative tax net operating loss deduction' means the net operating loss deduction allowable for the taxable year under section 172, except that in determining the amount of such deduction—

"(A) in the case of taxable years beginning after December 31, 1982, section 172(b)(2) shall be applied by substituting 'alternative minimum taxable income' for 'taxable income' each place it appears, and

"(B) the net operating loss (within the meaning of section 172(c)) for any loss year shall be adjusted as provided in paragraph (2).

"(2) Adjustments to net operating loss computation.—

"(A) Post-1982 loss years.—In the case of a loss year beginning after December 31, 1982, the net operating loss for such year under section 172(c) shall—

"(i) be reduced by the amount of the items of tax preference arising in such year which are taken into account in computing the net operating loss, and

"(ii) be computed by taking into account only itemized deductions which are alternative tax itemized de-

ductions for the taxable year and which are otherwise described in section 172(c).

"(B) PRE-1983 YEARS.—In the case of loss years beginning before January 1, 1983, the amount of the net operating loss which may be carried over to taxable years beginning after December 31, 1982, for purposes of subparagraph (A), shall be equal to the amount which may be carried from the loss year to the first taxable year of the taxpayer beginning after December 31, 1982.

"(e) ALTERNATIVE TAX ITEMIZED DEDUCTIONS.—For purposes of this section—

"(1) IN GENERAL.—The term 'alternative tax itemized deductions' means an amount equal to the sum of any amount allowable as a deduction for the taxable year (other than a deduction allowable in computing adjusted gross income) under—

"(A) section 165(a) for losses described in subsection (c)(3) or (d) of section 165,

"(B) section 170 (relating to charitable deductions),

"(C) section 213 (relating to medical deductions),

"(D) this chapter for qualified interest, or

"(E) section 691(c) (relating to deduction for estate tax).

"(2) AMOUNTS WHICH MAY BE CARRIED OVER.—No amount shall be taken into account under paragraph (1) to the extent such amount may be carried to another taxable year for purposes of the regular tax.

"(3) QUALIFIED INTEREST.—The term 'qualified interest' means the sum of—

"(A) any qualified housing interest, and

"(B) any amount allowed as a deduction for interest (other than qualified housing interest) to the extent such amount does not exceed the qualified net investment income of the taxpayer for the taxable year.

"(4) QUALIFIED HOUSING INTEREST.—

"(A) IN GENERAL.—The term 'qualified housing interest' means interest which is paid or accrued during the taxable year on indebtedness which is incurred in acquiring, constructing, or substantially rehabilitating any property which—

"(i) is the principal residence (within the meaning of section 1034) of the taxpayer at the time such interest accrues or is paid, or

"(ii) is a qualified dwelling used by the taxpayer (or any member of his family within the meaning of section 267(c)(4)) during the taxable year.

"(B) QUALIFIED DWELLING.—The term 'qualified dwelling' means any—

"(i) house,

"(ii) apartment,

"(iii) condominium, or

"(iv) mobile home not used on a transient basis (within the meaning of section 7701(a)(19)(C)(v)),

including all structures or other property appurtenant thereto.

"(C) SPECIAL RULE FOR INDEBTEDNESS INCURRED BEFORE JULY 1, 1982.—The term 'qualified housing interest' includes interest paid or accrued on indebtedness which—

"(i) was incurred by the taxpayer before July 1, 1982, and

"(ii) is secured by property which, at the time such indebtedness was incurred, was—

"(I) the principal residence (within the meaning of section 1034) of the taxpayer, or

"(II) a qualified dwelling used by the taxpayer (or any member of his family (within the meaning of section 267(c)(4))).

"(5) QUALIFIED NET INVESTMENT INCOME.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'qualified net investment income' means the excess of—

"(i) qualified investment income, over

"(ii) qualified investment expenses.

"(B) QUALIFIED INVESTMENT INCOME.—The term 'qualified investment income' means the sum of—

"(i) investment income (within the meaning of section 163(d)(3)(B) other than clause (ii) thereof),

"(ii) any net capital gain attributable to the disposition of property held for investment, and

"(iii) the amount of items of tax preference described in paragraph (1) of section 57(a).

"(C) QUALIFIED INVESTMENT EXPENSES.—The term 'qualified investment expenses' means the deductions directly connected with the production of qualified investment income to the extent that—

"(i) such deductions are allowable in computing adjusted gross income, and

"(ii) such deductions are not items of tax preference.

"(6) SPECIAL RULES FOR ESTATES AND TRUSTS.—

"(A) IN GENERAL.—In the case of an estate or trust, the alternative tax itemized deductions for any taxable year includes the deductions allowable under sections 642(c), 651(a), and 661(a).

"(B) DETERMINATION OF ADJUSTED GROSS INCOME.—The adjusted gross income of an estate or trust shall be computed in the same manner as in the case of an individual, except that the deductions for costs paid or incurred in connection with the administration of the estate or trust shall be treated as allowable in arriving at adjusted gross income.

"(7) LIMITATION ON MEDICAL DEDUCTION.—In applying subparagraph (C) of paragraph (1), the amount allowable as a deduction under section 213 shall be determined by substituting '10 percent' for '5 percent' in section 213(a).

"(8) TREATMENT OF INTERESTS IN LIMITED PARTNERSHIPS AND SUBCHAPTER S CORPORATIONS.—

"(A) CERTAIN INTEREST TREATED AS NOT ALLOWABLE IN COMPUTING ADJUSTED GROSS INCOME.—Any amount allowable as a deduction for interest on indebtedness incurred or

continued to purchase or carry a limited business interest shall be treated as not allowable in computing adjusted gross income.

"(B) INCOME TREATED AS QUALIFIED INVESTMENT INCOME.—Any income derived from a limited business interest shall be treated as qualified investment income.

"(C) LIMITED BUSINESS INTEREST.—The term 'limited business interest' means an interest—

"(i) as a limited partner in a partnership, or

"(ii) as a shareholder in an electing small business corporation (as defined in section 1371(b)) if the taxpayer does not actively participate in the management of such corporation.

"(f) OTHER DEFINITIONS.—For purposes of this section—

"(1) EXEMPTION AMOUNT.—The term 'exemption amount' means—

"(A) $40,000 in the case of—

"(i) a joint return, or

"(ii) a surviving spouse (as defined in section 2(a)),

"(B) $30,000 in the case of an individual who—

"(i) is not a married individual (as defined in section 143), and

"(ii) is not a surviving spouse (as so defined), and

"(C) $20,000 in the case of—

"(i) a married individual (as so defined) who files a separate return, or

"(ii) an estate or trust.

"(2) REGULAR TAX.—The term 'regular tax' means the taxes imposed by this chapter for the taxable year (computed without regard to this section and without regard to the taxes imposed by sections 72(m)(5)(B), 72(q), 402(e), 408(f), 409(c), and 667(b)) reduced by the sum of the credits allowable under subpart A of part IV of this subchapter (other than under sections 31, 39, and 43). For purposes of this paragraph, the amount of the credits allowable under such subpart shall be determined without regard to this section."

(b) ITEMS OF TAX PREFERENCE.—

(1) IN GENERAL.—Subsection (a) of section 57 (relating to items of tax preference) is amended—

(A) by striking out paragraph (1) and inserting in lieu thereof the following new paragraph:

"(1) EXCLUSION OF INTEREST AND DIVIDENDS.—Any amount excluded from gross income for the taxable year under section 116 or 128.",

(B) by striking out paragraphs (5) and (6) and inserting in lieu thereof the following new paragraphs:

"(5) MINING EXPLORATION AND DEVELOPMENT COSTS.—With respect to each mine or other natural deposit (other than an oil or gas well) of the taxpayer, an amount equal to the excess of—

"(A) the amount allowable as a deduction under section 616(a) or 617, over

"(B) the amount which would have been allowable if the expenditures had been capitalized and amortized ratably

over the 10-year period beginning with the taxable year in which such expenditures were made.

"(6) CIRCULATION AND RESEARCH AND EXPERIMENTAL EXPENDITURES.—An amount equal to the excess of—

"(A) the amount allowable as a deduction under section 173 or 174(a) for the taxable year, over

"(B) the amount which would have been allowable for the taxable year if the circulation expenditures described in section 173 or the research and experimental expenditures described in section 174 had been capitalized and amortized ratably over the 10-year period beginning with the taxable year in which such expenditures were made.", and

(C) by striking out paragraph (10) and inserting in lieu thereof the following:

"(10) INCENTIVE STOCK OPTIONS.—With respect to the transfer of a share of stock pursuant to the exercise of an incentive stock option (as defined in section 422A), the amount by which the fair market value of the share at the time of exercise exceeds the option price."

(2) CONFORMING AMENDMENTS.—

(A) The next to last sentence of section 57(a) is amended by striking out "(3), (11), and (12)" and inserting in lieu thereof "(1), (3), (5), (6), (11), and (12)(A)".

(B) Section 57(a) is amended by striking out the last sentence.

(c) OPTIONAL 10-YEAR WRITEOFF OF CERTAIN TAX PREFERENCES—

(1) Section 58 (relating to rules for application of minimum tax) is amended by adding at the end thereof the following new subsection:

"(i) OPTIONAL 10-YEAR WRITEOFF OF CERTAIN TAX PREFERENCES.—

"(1) IN GENERAL.—For purposes of this title, in the case of an individual, any qualified expenditure to which an election under this paragraph applies shall be allowed as a deduction ratably over the 10-year period beginning with the taxable year in which such expenditure was made.

"(2) QUALIFIED EXPENDITURE.—For purposes of this subsection, the term 'qualified expenditure' means any amount which, but for an election under this subsection, would have been allowable as a deduction for the taxable year in which paid or incurred under—

"(A) section 173 (relating to circulation expenditures),

"(B) section 174(a) (relating to research and experimental expenditures),

"(C) section 263(c) (relating to intangible drilling and development expenditures),

"(D) section 616(a) (relating to development expenditures), or

"(E) section 617 (relating to deduction of certain mining exploration expenditures).

"(3) OTHER SECTIONS NOT APPLICABLE.—Except as provided in this subsection, no deduction shall be allowed under any other

section for any qualified expenditure to which an election under this subsection applies.

"(4) SPECIAL ELECTION FOR INTANGIBLE DRILLING AND DEVELOPMENT COSTS NOT ALLOCABLE TO INTEREST AS LIMITED PARTNER.—

"(A) IN GENERAL.—In the case of any nonlimited partnership intangible drilling costs to which an election under this paragraph applies—

"(i) the applicable percentage of such costs (adjusted as provided in section 48(q)) shall be allowed as a deduction for the taxable year in which paid or incurred and for each of the 4 succeeding taxable years, and

"(ii) such costs shall be treated, for purposes of determining the amount of the credit allowable under section 38 for the taxable year in which paid or incurred, as qualified investment (within the meaning of subsections (c) and (d) of section 46) with respect to property placed in service during such year.

"(B) APPLICABLE PERCENTAGE.—For purposes of subparagraph (A), the term 'applicable percentage' means the percentage determined in accordance with the following table:

"Taxable Year:	*Applicable percentage:*
1	*15*
2	*22*
3	*21*
4	*21*
5	*21.*

"(C) NONLIMITED PARTNERSHIP INTANGIBLE DRILLING COSTS.—For purposes of this paragraph, the term 'nonlimited partnership intangible drilling costs' means any qualified expenditure described in paragraph (2)(C) of an individual which is not allocable to such individual's interest as a limited partner in a limited partnership.

"(5) ELECTION.—

"(A) IN GENERAL.—An election may be made under this subsection with respect to any qualified expenditure.

"(B) REVOCABLE ONLY WITH CONSENT.—An election under this subsection with respect to any qualified expenditure may be revoked only with the consent of the Secretary.

"(C) TIME AND MANNER.—An election under this subsection shall be made at such time and in such manner as the Secretary shall by regulations prescribe.

"(D) PARTNERS.—In the case of a partnership, any election under this subsection shall be made separately by each partner with respect to the partner's allocable share of any qualified expenditure.

"(6) DISPOSITIONS.—

"(A) OIL, GAS, AND GEOTHERMAL PROPERTY.—In the case of any disposition of any oil, gas, or geothermal property to which section 1254 applies (determined without regard to this section)—

"(i) any deduction under paragraph (1) or (4)(A) with respect to costs which are allocable to such property

shall, for purposes of section 1254, be treated as a deduction allowable under section 263(c), and

"(ii) in the case of any credit allowable under section 38 by reason of paragraph (4)(B) which is allocable to such property, such disposition shall, for purposes of section 47, be treated as a disposition of section 38 recovery property which is not 3-year property.

"(B) APPLICATION OF SECTION 617(d).—In the case of any disposition of mining property to which section 617(d) applies (determined without regard to this subsection), any amount allowable as a deduction under paragraph (1) which is allocable to such property shall, for purposes of section 617(d), be treated as a deduction allowable under section 617(a).

"(7) AMOUNTS TO WHICH ELECTION APPLY NOT TREATED AS TAX PREFERENCE.—Any qualified expenditure to which an election under paragraph (1) or (4) applies shall not be treated as an item of tax preference under section 57(a)."

(2) Subsection (a) of section 1016 (relating to adjustments to basis) is amended by striking out "and" at the end of paragraph (23), by striking out the period at the end of paragraph (24) and inserting in lieu thereof ", and", and by adding at the end thereof the following new paragraph:

"(25) for amounts allowed as deductions under section 58(i) (relating to optional 10-year writeoff of certain tax preferences)."

(c) CONFORMING AMENDMENTS.—

(1) Section 56 (relating to corporate minimum tax) is amended—

(A) by striking out "person" each place it appears and inserting in lieu thereof "corporation",

(B) by striking out "one-half (or in the case of a corporation, an amount equal to)" in subsection (c),

(C) by striking out "sections 72(m)(5)(B), 402(e), 408(f), 531, and 541" in subsection (c) and inserting in lieu thereof "sections 531 and 541",

(D) by striking out "31, 39, 43, and 44G" in subsection (c) and inserting in lieu thereof "39 and 44G", and

(E) by striking out the section heading and inserting in lieu thereof the following:

"SEC. 56. CORPORATE MINIMUM TAX."

(2) The table of sections for part IV of subchapter A of chapter 1 is amended by striking out the item relating to section 56 and inserting in lieu thereof the following:

"Sec. 56. Corporate minimum tax."

(3) Section 58 (relating to rules for application of minimum taxes) is amended—

(A) by striking out subsection (a),

(B) by striking out subsection (c) and inserting in lieu thereof the following:

"(c) ESTATES AND TRUSTS.—In the case of an estate or trust, the items of tax preference for any taxable year shall be apportioned between the estate or trust and the beneficiaries in accordance with regulations prescribed by the Secretary.", and

(C) in subsection (g)—

(i) by striking out "paragraphs (6) and" in paragraph (1) and inserting in lieu thereof "paragraph", and

(ii) by striking out so much of paragraph (2) as precedes the last two sentences thereof and inserting in lieu thereof the following:

"(2) CAPITAL GAINS.—For purposes of section 56, the items of tax preference set forth in section 57(a)(9) which are attributable to sources within any foreign country or possession of the United States shall not be taken into account if preferential treatment is not accorded gain from the sale or exchange of capital assets (or property treated as capital assets)."

(4) Section 5(a)(4) is amended by striking out "sections 55 and 56" and inserting in lieu thereof "section 55".

(5) Section 511(d)(2) is amended by striking out "and section 56 (as the case may be)".

(6) Subparagraph (A) of section 897(a)(2) (relating to 20-percent minimum tax on nonresident alien individuals) is amended to read as follows:

"(A) IN GENERAL.—In the case of any nonresident alien individual, the amount determined under section 55(a)(1) for the taxable year shall not be less than 20 percent of the lesser of—

"(i) the individual's alternative minimum taxable income (as defined in section 55(b)) for the taxable year, or

"(ii) the individual's net United States real property gain for the taxable year."

(7) Sections 6015(d)(1), 6362(b)(2)(A), and 6654(g)(1) are each amended by striking out "or 56".

(8)(A) Sections 46(a)(4), 53(a), and 901(a) are each amended by striking out "(relating to minimum tax for tax preferences)" and inserting in lieu thereof "(relating to corporate minimum tax)".

(B) Subparagraph (A) of section 936(a)(3) is amended by striking out "(relating to minimum tax)" and inserting in lieu thereof "(relating to corporate minimum tax)".

(9)(A) Section 173 (relating to circulation expenditures) is amended—

(i) by striking out "Notwithstanding section 263" and inserting in lieu thereof

"(a) GENERAL RULE.—Notwithstanding section 263", and

(ii) by adding at the end thereof the following new subsection:

"(b) CROSS REFERENCE.—

"For election of 10-year amortization of expenditures allowable as a deduction under subsection (a), see section 58(i)."

(B) Subsection (e) of section 174 (relating to research and experimental expenditures) is amended—

(i) by striking out "For adjustments" and inserting in lieu thereof

"(1) For adjustments",

(ii) by adding at the end thereof the following new paragraph:

"(2) For election of 10-year amortization of expenditures allowable as a deduction under subsection (a), see section 58(i).", and

(iii) by striking out "Cross Reference" and inserting in lieu thereof "Cross References".

(C) Section 616 (relating to development expenditures) is amended by adding at the end thereof the following new subsection:

"(d) Cross Reference.—

"For election of 10-year amortization of expenditures allowable as a deduction under subsection (a), see section 58(i)."

(D) Section 617 (relating to deduction of certain mining exploration expenditures) is amended by adding at the end thereof the following new subsection:

"(j) Cross Reference.—

"For election of 10-year amortization of expenditures allowable as a deduction under this section, see section 58(i)."

(10) Subsection (a) of section 7701 (relating to definitions) is amended by adding at the end thereof the following new paragraph:

"(38) Joint return.—The term 'joint return' means a single return made jointly under section 6013 by a husband and wife."

(d) Effective Date.—

(1) In general.—The amendments made by this section shall apply to taxable years beginning after December 31, 1982.

(2) Special rule for pre-1983 section 56(b) tax deferrals.—The amendments made by subsection (c)(1) of this section to section 56(b) of the Internal Revenue Code of 1954 shall not apply to any net operating loss carryover from any taxable year beginning before January 1, 1983, which is attributable to any excess described in section 56(b)(1)(B) of such Code for such taxable year.

SEC. 202. LIMITATION ON MEDICAL DEDUCTION.

(a) General Rule.—Subsection (a) of section 213 (relating to deduction for medical, dental, etc., expenses) is amended to read as follows:

"(a) Allowance of Deduction.—There shall be allowed as a deduction the expenses paid during the taxable year, not compensated for by insurance or otherwise, for medical care of the taxpayer, his spouse, or a dependent (as defined in section 152), to the extent that such expenses exceed 5 percent of adjusted gross income."

(b) Treatment of Medicine and Drugs.—

(1) In general.—Subsection (b) of section 213 (relating to limitation with respect to medicine and drugs) is amended to read as follows:

"(b) Limitation With Respect to Medicine and Drugs.—An amount paid during the taxable year for medicine or a drug shall be taken into account under subsection (a) only if such medicine or drug is a prescribed drug or is insulin."

(2) Definition of prescribed drug.—Subsection (e) of section 213 is amended by inserting after paragraph (1) the following new paragraphs:

"(2) Prescribed drug.—The term 'prescribed drug' means a drug or biological which requires a prescription of a physician for its use by an individual.

"(3) Physician.—The term 'physician' has the meaning given to such term by section 1861(r) of the Social Security Act (42 U.S.C. 1395x(r))."

(3) Conforming amendments.—

(A) Subsection (e) of section 213 (as in effect before the amendment made by paragraph (2)) is amended by redesignating paragraphs (2), (3), and (4) as paragraphs (4), (5), and (6), respectively.

(B) Subsections (d), (e), and (f) of section 213 are redesignated as subsections (c), (d), and (e), respectively.

(C) Subsection (b) of section 105 is amended by striking out "section 213(e)" and inserting in lieu thereof "section 213(d)".

(c) Effective Dates.—

(1) Subsection (a).—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1982.

(2) Subsection (b).—The amendments made by subsection (b) shall apply to taxable years beginning after December 31, 1983.

SEC. 203. LIMITATION ON DEDUCTION FOR NONBUSINESS CASUALTY LOSSES.

(a) General Rule.—Section 165 (relating to losses) is amended by striking out subsection (h), by redesignating subsection (i) as subsection (j), and by inserting after subsection (g) the following new subsections:

"(h) Casualty and Theft Losses.—

"(1) General rule.—Any loss of an individual described in subsection (c)(3) shall be allowed for any taxable year only to the extent that—

"(A) the amount of loss to such individual arising from each casualty, or from each theft, exceeds $100, and

"(B) the aggregate amount of all such losses sustained by such individual during the taxable year (determined after application of subparagraph (A)) exceeds 10 percent of the adjusted gross income of the individual.

"(2) Special rules.—

"(A) Joint returns.—For purposes of the $100 and 10 percent limitations described in paragraph (1), a husband and wife making a joint return for the taxable year shall be treated as one individual.

"(B) Coordination with estate tax.—No loss described in subsection (c)(3) shall be allowed if, at the time of filing the return, such loss has been claimed for estate tax purposes in the estate tax return.

"(i) Disaster Losses.—

"(1) Election to take deduction for preceding year.—Notwithstanding the provisions of subsection (a), any loss attributable to a disaster occurring in an area subsequently deter-

mined by the President of the United States to warrant assistance by the Federal Government under the Disaster Relief Act of 1974 may, at the election of the taxpayer, be taken into account for the taxable year immediately preceding the taxable year in which the disaster occurred.

"(2) YEAR OF LOSS.—If an election is made under this subsection, the casualty resulting in the loss shall be treated for purposes of this title as having occurred in the taxable year for which the deduction is claimed.

"(3) AMOUNT OF LOSS.—The amount of the loss taken into account in the preceding taxable year by reason of paragraph (1) shall not exceed the uncompensated amount determined on the basis of the facts existing at the date the taxpayer claims the loss."

(b) CONFORMING AMENDMENT.—Subsection (c) of section 165 (relating to limitation on losses of individuals) is amended—

(1) by inserting "except as provided in subsection (h)," before "losses" the first place it appears in paragraph (3) thereof, and

(2) by striking out the last three sentences.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1982. Such amendments shall also apply to the taxpayer's last taxable year beginning before January 1, 1983, solely for purposes of determining the amount allowable as a deduction with respect to any loss taken into account for such year by reason of an election under section 165(i) of the Internal Revenue Code of 1954 (as amended by this section).

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Subtitle B—Provisions Primarily Relating to Business

PART I—REDUCTION IN CERTAIN DEDUCTIONS AND CREDITS

SEC. 204. 15 PERCENT REDUCTION IN CERTAIN CORPORATE PREFERENCE ITEMS.

(a) In General.—Subchapter B of chapter 1 (relating to computation of taxable income) is amended by adding at the end thereof the following new part:

"PART XI—SPECIAL RULES RELATING TO CORPORATE PREFERENCE ITEMS

"Sec. 291. Special rules relating to corporate preference items.

"SEC. 291. SPECIAL RULES RELATING TO CORPORATE PREFERENCE ITEMS.

"(a) 15-Percent Reduction in Certain Preference Items, Etc.—For purposes of this subtitle, in the case of an applicable corporation—

"(1) Section 1250 capital gain treatment.—In the case of section 1250 property which is disposed of during the taxable year, 15 percent of the excess (if any) of—

"(A) the amount which would be treated as ordinary income if such property was section 1245 property or section 1245 recovery property, over

"(B) the amount treated as ordinary income under section 1250,

shall be treated as gain which is ordinary income and shall be recognized notwithstanding any other provision of this title.

"(2) Reduction in percentage depletion.—In the case of iron ore and coal (including lignite), the amount allowable as a deduction under section 613 with respect to any property (as defined in section 614) shall be reduced by 15 percent of the amount of the excess (if any) of—

"(A) the amount of the deduction allowable under section 613 for the taxable year (determined without regard to this paragraph), over

"(B) the adjusted basis of the property at the close of the taxable year (determined without regard to the depletion deduction for the taxable year).

"(3) Certain financial institution preference items.—The amount allowable as a deduction under this chapter (determined without regard to this section) with respect to any financial institution preference item shall be reduced by 15 percent.

"(4) Certain deferred DISC income.—If an applicable corporation is a shareholder of a DISC, in the case of taxable years

beginning after December 31, 1982, section 995(b)(1)(F)(i) shall be applied with respect to such corporation by substituting '57.5 percent' for 'one-half'.

"(5) AMORTIZATION OF POLLUTION CONTROL FACILITIES.—If an election is made under section 169 with respect to any certified pollution control facility, the amortizable basis of such facility for purposes of such section shall be reduced by 15 percent.

"(b) SPECIAL RULES FOR TREATMENT OF INTANGIBLE DRILLING COSTS AND MINERAL EXPLORATION AND DEVELOPMENT COSTS.—For purposes of this subtitle, in the case of an applicable corporation—

"(1) IN GENERAL.—The amount allowable as a deduction for any taxable year (determined without regard to this section)—

"(A) under section 263(c) in the case of an integrated oil company, or

"(B) under section 616(a) or 617,

shall be reduced by 15 percent.

"(2) Special rule for amounts not allowable as deductions under paragraph (1).—

"(A) INTANGIBLE DRILLING COSTS.—The amount not allowable as a deduction under section 263(c) for any taxable year by reason of paragraph (1) shall be allowable as a deduction ratably over the 36-month period beginning with the month in which the costs are paid or incurred.

"(B) MINERAL EXPLORATION AND DEVELOPMENT COSTS.—In the case of any amount not allowable as a deduction under section 616(a) or 617 for any taxable year by reason of paragraph (1)—

"(i) the applicable percentage of the amount not so allowable as a deduction shall be allowable as a deduction for the taxable year in which the costs are paid or incurred and in each of the 4 succeeding taxable years, and

"(ii) such costs shall be treated, for purposes of determining the amount of the credit allowable under section 38 for the taxable year in which paid or incurred, as qualified investment (within the meaning of subsections (c) and (d) of section 46) with respect to property placed in service during such year.

"(3) APPLICABLE PERCENTAGE.—For purposes of paragraph (2)(B), the term 'applicable percentage' means the percentage determined in accordance with the following table:

"Taxable Year:	*Applicable Percentage:*
1	*15*
2	*22*
3	*21*
4	*21*
5	*21.*

"(4) DISPOSITIONS.—

"(A) OIL, GAS, AND GEOTHERMAL PROPERTY.—In the case of any disposition of any oil, gas, or geothermal property to which section 1254 applies (determined without regard to this section) any deduction under paragraph (2)(A) with respect to intangible drilling and development costs under

section 263(c) which are allocable to such property shall, for purposes of section 1254, be treated as a deduction allowable under section 263(c).

"(B) Application of section 617(d).—In the case of any disposition of mining property to which section 617(d) applies (determined without regard to this section), any amount allowable as a deduction under paragraph (2)(B) which is allocable to such property shall, for purposes of section 617(d), be treated as a deduction allowable under section 617(a).

"(C) Recapture of investment credit.—In the case of any disposition of any property to which the credit allowable under section 38 by reason of paragraph (2)(B) is allocable, such disposition shall, for purposes of section 47, be treated as a disposition of section 38 recovery property which is not 3-year property.

"(5) Integrated oil company defined.—For purposes of this subsection, the term 'integrated oil company' means, with respect to any taxable year, any producer (within the meaning of section 4996(a)(1)) of crude oil other than an independent producer (within the meaning of section 4992(b)).

"(6) Coordination with cost depletion.—The portion of the adjusted basis of any property which is attributable to intangible drilling and development costs or mining exploration and development costs shall not be taken into account for purposes of determining depletion under section 611.

"(c) Special Rules Relating to Pollution Control Facilities.—For purposes of this subtitle—

"(1) Accelerated cost recovery deduction.—For purposes of subclause (I) of section 168(d)(1)(A)(ii), a taxpayer shall not be treated as electing the amortization deduction under section 169 with respect to that portion of the basis not taken into account under section 169 by reason of subsection (a)(5).

"(2) 1250 recapture.—Subsection (a)(1) shall not apply to any section 1250 property which is part of a certified pollution control facility (within the meaning of section 169(d)(1)) with respect to which an election under section 169 was made.

"(d) Special Rule for Real Estate Investment Trusts.—In the case of a real estate investment trust (as defined in section 856), the difference between the amounts described in subparagraphs (A) and (B) of subsection (a)(1) shall be reduced to the extent that a capital gain dividend (as defined in section 857(b)(3)(C), applied without regard to this section) is treated as paid out of such difference. Any capital gain dividend treated as having been paid out of such difference to a shareholder which is an applicable corporation retains its character in the hands of the shareholder as gain from the disposition of section 1250 property for purposes of applying subsection (a)(1) to such shareholder.

"(e) Definitions.—For purposes of this section—

"(1) Financial institution preference item.—The term 'financial institution preference item' includes the following:

"(A) Excess reserves for losses on bad debts of financial institutions.—In the case of a financial institution to which section 585 or 593 applies, the excess of—

"(i) the amount which would, but for this section, be allowable as a deduction for the taxable year for a reasonable addition to a reserve for bad debts, over

"(ii) the amount which would have been allowable had such institution maintained its bad debt reserve for all taxable years on the basis of actual experience.

"(B) Interest on debt to carry tax-exempt obligations acquired after December 31, 1982.—

"(i) In general.—In the case of a financial institution to which section 585 or 593 applies, the amount of interest on indebtedness incurred or continued to purchase or carry obligations acquired after December 31, 1982, the interest on which is exempt from taxes for the taxable year, to the extent that a deduction would (but for this paragraph) be allowable with respect to such interest for such taxable year.

"(ii) Determination of interest allocable to indebtedness on tax-exempt obligations.—Unless the taxpayer (under regulations prescribed by the Secretary) establishes otherwise, the amount determined under clause (i) shall be an amount which bears the same ratio to the aggregate amount allowable (determined without regard to this section) to the taxpayer as a deduction for interest for the taxable year as—

"(I) the taxpayer's average adjusted basis (within the meaning of section 1016) of obligations described in clause (i), bears to

"(II) such average adjusted basis for all assets of the taxpayer.

"(2) Applicable corporation.—For purposes of this section, the term 'applicable corporation' means any corporation other than an electing small business corporation (as defined in section 1371(b)).

"(3) Section 1245 and 1250 property.—The terms 'section 1245 property', 'section 1245 recovery property', and 'section 1250 property' have the meanings given such terms by sections 1245(a)(3), 1245(a)(5), and 1250(c), respectively."

(b) Coordination With Minimum Tax.—Section 57(b) (relating to adjusted itemized deductions) is amended to read as follows:

"(b) Application With Section 291.—

"(1) In general.—In the case of any item of tax preference of an applicable corporation described in—

"(A) paragraph (4) or (7) of subsection (a), or

"(B) paragraph (8) of subsection (a) (but only to the extent such item is allocable to a deduction for depletion for iron ore and coal (including lignite)),

only 71.6 percent of the amount of such item of tax preference (determined without regard to this subsection) shall be taken into account as an item of tax preference.

"(2) Certain capital gains.—In determining the net capital gain of any applicable corporation for purposes of paragraph (9)(B) of subsection (a), there shall be taken into account only 71.6 percent of any gain from the sale or exchange of section

1250 property which is equal to 85 percent of the excess determined under section 291(a)(1) with respect to such property.

"(3) APPLICABLE CORPORATION DEFINED.—For purposes of this subsection, the term 'applicable corporation' has the meaning given such term by section 291(e)(2)."

(c) CONFORMING AMENDMENTS.—

(1) Subsection (c) of section 263 (relating to intangible drilling and development costs) is amended by adding at the end thereof the following new sentence: "This subsection shall not apply with respect to any costs to which any deduction is allowed under section 58(i) or 291."

(2) The table of parts for subchapter B of chapter 1 is amended by adding at the end thereof the following:

"Part XI. Special rules relating to corporate preference items."

(d) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section shall apply to taxable years beginning after December 31, 1982.

(2) 1250 GAIN.—Section 291(a)(1) of the Internal Revenue Code of 1954 shall apply to sales or other dispositions after December 31, 1982, in taxable years ending after such date.

(3) POLLUTION CONTROL FACILITIES.—Section 291(a)(5) of such Code shall apply to property placed in service after December 31, 1982, in taxable years ending after such date.

(4) DRILLING AND MINING COSTS.—Section 291(b) of such Code shall apply to expenditures after December 31, 1982, in taxable years ending after such date.

(5) REDUCTION IN PERCENTAGE DEPLETION FOR COAL AND IRON ORE.—Section 291(a)(2) of such Code shall apply to taxable years beginning after December 31, 1983.

(6) MINIMUM TAX.—The amendment made by subsection (b) shall apply to taxable years ending after December 31, 1982, with respect to items of tax preference described in section 57(b) of such Code to which section 291 of such Code applies; except that in the case of an item described in section 291(a)(2) of such Code, such amendment shall apply to taxable years beginning after December 31, 1983.

SEC. 205. AMENDMENTS TO INVESTMENT CREDIT.

(a) BASIS ADJUSTMENT TO REFLECT INVESTMENT TAX CREDIT.—

(1) IN GENERAL.—Section 48 (relating to definitions and special rules involving section 38 property) is amended by redesignating subsection (q) as subsection (r) and by inserting after subsection (p) the following new subsection:

"(q) BASIS ADJUSTMENT TO SECTION 38 PROPERTY.—

"(1) IN GENERAL.—For purposes of this subtitle, if a credit is determined under section 46(a)(2) with respect to section 38 property, the basis of such property shall be reduced by 50 percent of the amount of the credit so determined.

"(2) CERTAIN DISPOSITIONS.—If during any taxable year there is a recapture amount determined with respect to any section 38 property the basis of which was reduced under paragraph (1), the basis of such property (immediately before the event resulting in such recapture) shall be increased by an amount equal to

50 percent of such recapture amount. For purposes of the preceding sentence, the term 'recapture amount' means any increase in tax (or adjustment in carrybacks or carryovers) determined under section 47.

"(3) SPECIAL RULE FOR QUALIFIED REHABILITATED BUILDINGS.—In the case of any credit determined under section 46(a)(2) for any qualified rehabilitation expenditure in connection with a qualified rehabilitated building other than a certified historic structure, paragraphs (1) and (2) shall be applied without regard to the phrase '50 percent of'.

"(4) ELECTION OF REDUCED CREDIT IN LIEU OF BASIS ADJUSTMENT FOR REGULAR PERCENTAGE.—

"(A) IN GENERAL.—If the taxpayer elects to have this paragraph apply with respect to any recovery property—

"(i) paragraphs (1) and (2) shall not apply to so much of the credit determined under section 46(a)(2) with respect to such property as is attributable to the regular percentage set forth in section 46(a)(2)(B); and

"(ii) the amount of the credit allowable under section 38 with respect to such property shall be determined under subparagraph (B).

"(B) REDUCTION IN CREDIT.—In the case of any recovery property to which an election under subparagraph (A) applies—

"(i) solely for the purposes of applying the regular percentage, the applicable percentage under subsection (c) or (d) of section 46 shall be deemed to be 100 percent, and

"(ii) notwithstanding section 46(a)(2)(B), the regular percentage shall be—

"(I) 8 percent in the case of recovery property other than 3-year property, or

"(II) 4 percent in the case of recovery property which is 3-year property.

For purposes of the preceding sentence, RRB replacement property (within the meaning of section 168(f)(3)(B)) shall be treated as property which is not 3-year property.

"(C) TIME AND MANNER OF MAKING ELECTION.—

"(i) IN GENERAL.—An election under this subsection with respect to any property shall be made on the taxpayer's return of the tax imposed by this chapter for the taxpayer's taxable year in which such property is placed in service (or in the case of property to which an election under section 46(d) applies, for the first taxable year for which qualified progress expenditures were taken into account with respect to such property).

"(ii) REVOCABLE ONLY WITH CONSENT.—An election under this subsection with respect to any property, once made, may be revoked only with the consent of the Secretary.

"(5) RECAPTURE OF REDUCTIONS.—

"(A) IN GENERAL.—For purposes of sections 1245 and 1250, any reduction under this subsection shall be treated as a deduction allowed for depreciation.

"(B) SPECIAL RULE FOR SECTION 1250.—For purposes of section 1250(b), the determination of what would have been the depreciation adjustments under the straight line method shall be made as if there had been no reduction under this section."

(2) ALLOWANCE OF DEDUCTION FOR CERTAIN UNUSED INVESTMENT CREDITS.—Part VI of subchapter B of chapter 1 (relating to itemized deductions for individuals and corporations) is amended by adding at the end thereof the following new section:

"SEC. 196. DEDUCTION FOR CERTAIN UNUSED INVESTMENT CREDITS.

"(a) ALLOWANCE OF DEDUCTIONS.—If—

"(1) the amount of the credit determined under section 46(a)(2) for any taxable year exceeds the limitation provided by section 46(a)(3) for such taxable year, and

"(2) the amount of such excess has not, after the application of section 46(b), been allowed to the taxpayer as a credit under section 38 for any taxable year,

then an amount equal to 50 percent of the amount of such excess (to the extent attributable to property the basis of which is reduced under section 48(q)) not so allowed as a credit shall be allowed to the taxpayer as a deduction for the first taxable year following the last taxable year in which such excess could under section 46(b) have been allowed as a credit.

"(b) TAXPAYERS DYING OR CEASING TO EXIST.—If a taxpayer dies or ceases to exist prior to the first taxable year following the last taxable year in which the excess described in subsection (a) could under section 46(b) have been allowed as a credit, the amount described in subsection (a), or the proper portion thereof, shall, under regulations prescribed by the Secretary, be allowed to the taxpayer as a deduction for the taxable year in which such death or cessation occurs.

"(c) SPECIAL RULE FOR QUALIFIED REHABILITATED BUILDINGS.—In the case of any credit to which section 48(q)(3) applies, subsection (a) shall be applied without regard to the phrase '50 percent of'."

(3) BASIS ADJUSTMENT NOT TAKEN INTO ACCOUNT FOR PURPOSES OF EARNINGS AND PROFITS.—Section 312(k) (relating to effect of depreciation on earnings and profits) is amended by adding at the end thereof the following new paragraph:

"(5) BASIS ADJUSTMENT NOT TAKEN INTO ACCOUNT.—In computing the earnings and profits of a corporation for any taxable year, the allowance for depreciation (and amortization, if any) shall be computed without regard to any basis adjustment under section 48(q)."

(4) SPECIAL RULES FOR CERTAIN LEASED PROPERTY.—Section 48(d) (relating to certain leased property) is amended by adding at the end thereof the following new paragraph:

"(5) COORDINATION WITH BASIS ADJUSTMENT.—In the case of any property with respect to which an election is made under this subsection—

"(A) subsection (q) (other than paragraph (4)) shall not apply with respect to such property,

"(B) the lessee of such property shall include ratably in gross income over the shortest recovery period which could be applicable under section 168 with respect to such property an amount equal to 50 percent of the amount of the credit allowable under section 38 to the lessee with respect to such property, and

"(C) in the case of a disposition of such property to which section 47 applies, this paragraph shall be applied in accordance with regulations prescribed by the Secretary."

(5) CONFORMING AMENDMENTS.—

(A) Section 48(g) (relating to special rules for qualified rehabilitated buildings) is amended by striking out paragraph (5).

(B) Paragraph (24) of section 1016(a) (relating to adjustments to basis) is amended by striking out "section 48(g)(5)" and inserting in lieu thereof "section 48(q)".

(C) The table of sections for part VI of subchapter B of chapter 1 is amended by adding at the end thereof the following new item:

"Sec. 196. Deduction for certain unused investment credits."

(b) INVESTMENT CREDIT LIMITED TO 85 PERCENT OF TAX LIABILITY INSTEAD OF 90 PERCENT.—

(1) IN GENERAL.—Subparagraph (B) of section 46(a)(3) (relating to limitation based on amount of tax) is amended to read as follows:

"(B) 85 percent of so much of the liability for tax for the taxable year as exceeds $25,000."

(2) TECHNICAL AMENDMENTS.—

(A) Subsection (a) of section 46 is amended by striking out paragraphs (7) and (8) and by redesignating paragraph (9) as paragraph (7).

(B) Clause (i) of section 46(a)(7)(B), as redesignated by subparagraph (A), is amended to read as follows:

"(i) paragraph (3)(B) shall be applied by substituting '100 percent' for '85 percent', and".

(C) Subparagraph (B) of section 46(a)(7), as redesignated by subparagraph (A), is amended by striking clause (ii) and by redesignating clause (iii) as clause (ii).

(c) EFFECTIVE DATES.—

(1) SUBSECTION (a).—

(A) GENERAL RULE.—Except as otherwise provided in this paragraph, the amendments made by subsection (a) shall apply to periods after December 31, 1982, under rules similar to the rules of section 48(m) of the Internal Revenue Code of 1954.

(B) EXCEPTION.—The amendments made by subsection (a) shall not apply to any property which—

(i) is constructed, reconstructed, erected, or acquired pursuant to a contract which was entered into after August 13, 1981, and was, on July 1, 1982, and at all times thereafter, binding on the taxpayer,

(ii) is placed in service after December 31, 1982, and before January 1, 1986,

(iii) with respect to which an election under section 168(f)(8)(A) of such Code is not in effect at any time, and

(iv) is not described in section 167(l)(3)(A) of such Code.

(C) SPECIAL RULE FOR INTEGRATED MANUFACTURING FACILITIES.—

(i) IN GENERAL.—In the case of any integrated manufacturing facility, the requirements of clause (i) of subparagraph (B) shall be treated as met if—

(I) the on-site construction of the facility began before July 1, 1982, and

(II) during the period beginning after August 13, 1981, and ending on July 1, 1982, the taxpayer constructed (or entered into binding contracts for the construction of) more than 20 percent of the cost of such facility.

(ii) INTEGRATED MANUFACTURING FACILITY.—For purposes of clause (i), the term 'integrated manufacturing facility' means 1 or more facilities—

(I) located on a single site,

(II) for the manufacture of 1 or more manufactured products from raw materials by the application of 2 or more integrated manufacturing processes.

(D) SPECIAL RULE FOR HISTORIC STRUCTURES.—In the case of any certified historic structure (as defined in section 48(g)(3) of the Internal Revenue Code of 1954), clause (i) of subparagraph (B) shall be applied by substituting "December 31, 1980" for "August 13, 1981."

(E) CERTAIN PROJECTS WITH RESPECT TO HISTORIC STRUCTURES.—In the case of any certified historic structure (as so defined), the requirements of clause (i) of subparagraph (B) shall be treated as met with respect to such property—

(i) if the rehabilitation begins after December 31, 1980, and before July 1, 1982, or

(ii) if—

(I) before July 1, 1982, a public offering with respect to interests in such property was registered with the Securities and Exchange Commission,

(II) before such date an application with respect to such property was filed under section 8 of the United States Housing Act of 1937, and

(III) such property is placed in service before July 1, 1984.

(2) SUBSECTION (b).—The amendments made by subsection (b) shall apply to taxable years beginning after December 31, 1982.

SEC. 206. REPEAL OF 1985 AND 1986 INCREASES IN ACCELERATED COST RECOVERY DEDUCTIONS.

(a) IN GENERAL.—Paragraph (1) of section 168(b) (relating to amount of accelerated cost recovery deduction) is amended—

(1) by striking out "tables" and inserting in lieu thereof "table";

(2) by striking out:

"(A) FOR PROPERTY PLACED IN SERVICE AFTER DECEMBER 31, 1980, AND BEFORE JANUARY 1, 1985.—"; and

(3) by striking out subparagraphs (B) and (C).

(b) CONFORMING AMENDMENTS.—Paragraph (4) of section 168(e) (relating to property excluded from application of section) is amended—

(1) by striking out subparagraph (H); and

(2) by striking out "1986" in the heading thereof and inserting in lieu thereof "1981".

SEC. 207. SECTION 189 MADE APPLICABLE TO CERTAIN CORPORATIONS FOR NONRESIDENTIAL REAL PROPERTY.

(a) IN GENERAL.—Subsection (a) of section 189 is amended to read as follows:

"(a) CAPITALIZATION OF CONSTRUCTION PERIOD INTEREST AND TAXES.—Except as otherwise provided in this section or in section 266 (relating to carrying charges), no deduction shall be allowed for real property construction period interest and taxes."

(b) EXCLUSION OF CERTAIN PROPERTY.—Subsection (d) of section 189 (relating to certain property excluded) is amended—

(1) by striking out "or" at the end of paragraph (1),

(2) by redesignating paragraph (2) as paragraph (3), and

(3) by inserting after paragraph (1) the following new paragraph:

"(2) residential real property (other than low income housing) acquired, constructed, or carried by a corporation other than an electing small business corporation (within the meaning of section 1371(b)), a personal holding company (within the meaning of section 542), or a foreign personal holding company (within the meaning of section 552), or".

(c) ALLOCATION OF INTEREST.—Paragraph (1) of section 189(e) (relating to construction period interest and taxes) is amended by adding at the end thereof the following sentence: "The Secretary shall prescribe regulations which provide for the allocation of interest to real property under construction."

(d) CONFORMING AMENDMENT.—Paragraph (1) of section 189(e) (relating to construction period interest and taxes) is amended—

(1) by striking out "construction period interest and taxes" and inserting in lieu thereof "real property construction period interest and taxes", and

(2) by striking out the caption thereof and inserting in lieu thereof:

"(1) REAL PROPERTY CONSTRUCTION PERIOD INTEREST AND TAXES.—".

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1982, with respect to construction which commences after such date.

(2) CERTAIN PLANNED CONSTRUCTION.—The amendments made by this section shall not apply with respect to construction of property which is used in a trade or business described

in section 48(a)(3)(B) of the Internal Revenue Code of 1954 or which is a hospital or nursing home if—

(A) such construction is conducted pursuant to a written plan of the taxpayer which was in existence on July 1, 1982, and as to which approval from a governmental unit has been requested in writing, and

(B) such construction commences before January 1, 1984, and shall not apply to the Alaska Natural Gas Transportation System (15 U.S.C. 719) and its related facilities.

PART II—LEASING

SEC. 208. LIMITATIONS AND ADDITIONAL REQUIREMENTS ON LEASES UNDER THE ACCELERATED COST RECOVERY SYSTEM.

(a) LIMITATIONS ON LEASES UNDER THE ACCELERATED COST RECOVERY SYSTEM.—

(1) IN GENERAL.—Section 168 (relating to the accelerated cost recovery system) is amended by redesignating subsection (i) as subsection (j) and by inserting after subsection (h) the following new subsection:

"(i) LIMITATIONS RELATING TO LEASES OF QUALIFIED LEASED PROPERTY.—For purposes of this subtitle, in the case of safe harbor lease property, the following limitations shall apply:

"(1) LESSOR MAY NOT REDUCE TAX LIABILITY BY MORE THAN 50 PERCENT.—

"(A) IN GENERAL.—The aggregate amount allowable as deductions or credits for any taxable year which are allocable to all safe harbor lease property with respect to which the taxpayer is the lessor may not reduce the liability for tax of the taxpayer for such taxable year (determined without regard to safe harbor lease items) by more than 50 percent of such liability.

"(B) CARRYOVER OF AMOUNTS NOT ALLOWABLE AS DEDUCTIONS OR CREDITS.—Any amount not allowable as a deduction or credit under subparagraph (A)—

"(i) may be carried over to any subsequent taxable year, and

"(ii) shall be treated as a deduction or credit allocable to safe harbor lease property in such subsequent taxable year.

"(C) ALLOCATION AMONG DEDUCTIONS AND CREDITS.—The Secretary shall prescribe regulations for determining the amount—

"(i) of any deduction or credit allocable to safe harbor lease property for any taxable year to which subparagraph (A) applies, and

"(ii) of any carryover of any such deduction or credit under subparagraph (B) to any subsequent taxable year.

"(D) LIABILITY FOR TAX AND SAFE HARBOR LEASE ITEMS DEFINED.—For purposes of this paragraph—

"(i) LIABILITY FOR TAX DEFINED.—Except as provided in this subparagraph, the term 'liability for tax' means

the tax imposed by this chapter, reduced by the sum of the credits allowable under subpart A of part IV of subchapter A of this chapter.

"(ii) SAFE HARBOR LEASE ITEMS DEFINED.—The term 'safe harbor lease items' means any of the following items which are properly allocable to safe harbor lease property with respect to which the taxpayer is the lessor:

"(I) Any deduction or credit allowable under this chapter (other than any deduction for interest).

"(II) Any rental income received by the taxpayer from any lessee of such property.

"(III) Any interest allowable as a deduction under this chapter on indebtedness of the taxpayer (or any related person within the meaning of subsection (e)(4)(D)) which is paid or incurred to the lessee of such property (or any person so related to the lessee).

"(iii) CERTAIN TAXES NOT INCLUDED.—The term 'tax imposed by this chapter' shall not include any tax treated as not imposed by this chapter under the last sentence of section 53(a) (other than the tax imposed by section 56).

"(2) METHOD OF COST RECOVERY.—The deduction allowable under subsection (a) with respect to any safe harbor lease property shall be determined by using the 150 percent declining balance method, switching to the straight-line method at a time to maximize the deduction (with a half-year convention in the first recovery year and without regard to salvage value) and a recovery period determined in accordance with the following table:

"In the case of:	*The recovery period is:*
3-year property	*5 years.*
5-year property	*8 years.*
10-year property	*15 years.*

"(3) INVESTMENT CREDIT ALLOWED ONLY OVER 5-YEAR PERIOD.—In the case of any credit which would otherwise be allowable under section 38 with respect to any safe harbor lease property for any taxable year (determined without regard to this paragraph), only 20 percent of the amount of such credit shall be allowable in such taxable year and 20 percent of such amount shall be allowable in each of the succeeding 4 taxable years.

"(4) NO CARRYBACKS OF CREDIT OR NET OPERATING LOSS ALLOCABLE TO ELECTED QUALIFIED LEASED PROPERTY.—

"(A) CREDIT CARRYBACKS.—In determining the amount of any credit allowable under subpart A of part IV of subchapter A of this chapter which may be carried back to any preceding taxable year—

"(i) the liability for tax for the taxable year from which any such credit is to be carried shall be reduced first by any credit not properly allocable to safe harbor lease property, and

"(ii) no credit which is properly allocable to safe harbor lease property shall be taken into account in determining the amount of any credit which may be carried back.

"(B) Net operating loss carrybacks.—The net operating loss carryback provided in section 172(b) for any taxable year shall be reduced by that portion of the amount of such carryback which is properly allocable to the items described in paragraph (1)(D)(ii) with respect to all safe harbor lease property with respect to which the taxpayer is the lessor.

"(5) Limitation on deduction for interest paid by the lessor to the lessee.—In the case of interest described in paragraph (1)(D)(ii)(III), the amount allowable as a deduction for any taxable year with respect to such interest shall not exceed the amount which would have been computed if the rate of interest under the agreement were equal to the rate of interest in effect under section 6621 at the time the agreement was entered into.

"(6) Computation of taxable income of lessee for purposes of percentage depletion.—

"(A) In general.—For purposes of section 613 or 613A, the taxable income of any taxpayer who is a lessee of any safe harbor lease property shall be computed as if the taxpayer was the owner of such property, except that the amount of the deduction under subsection (a) of this section shall be determined after application of paragraph (2) of this subsection.

"(B) Coordination with crude oil windfall profit tax.—Section 4988(b)(3)(A) shall be applied without regard to subparagraph (A).

"(7) Transitional rule for application of paragraph (1) to certain transactions.—In the case of any deduction or credit with respect to—

"(A) any transitional safe harbor lease property (within the meaning of section 208(d)(3) of the Tax Equity and Fiscal Responsibility Act of 1982), or

"(B) any other safe harbor lease property placed in service during 1982 and to which paragraph (1) does not apply,

paragraph (1) shall not operate to disallow any such deduction or credit for the taxable year for which such deduction or credit would otherwise be allowable but deductions and credits with respect to such property shall be taken into account first in determining whether any deduction or credit is allowable under paragraph (1) with respect to any other safe harbor lease property.

"(8) Safe harbor lease property.—For purposes of this section, the term 'safe harbor lease property' means qualified leased property with respect to which an election under section 168(f)(8) is in effect."

(2) Conforming amendment.—

(A) Subparagraph (A) of section 168(f)(8) (relating to special rules for leases) is amended by inserting "except as provided in subsection (i)," before "for purposes of this subtitle".

(B) Subparagraph (D) of section 47(a)(5) (relating to certain dispositions, etc., of section 38 property) is amended by adding at the end thereof the following new sentence: "If, prior to a disposition to which this subsection applies, any portion of any credit is not allowable with respect to any property by reason of section 168(i)(3), such portion shall be treated (for purposes of this subparagraph) as not having been used to reduce tax liability."

(b) ADDITIONAL REQUIREMENTS TO QUALIFY AS LEASE FOR PURPOSES OF ACCELERATED COST RECOVERY.—

(1) RELATED PERSONS MAY NOT QUALIFY AS LESSORS.—Subclause (I) of section 168(f)(8)(B)(i) (relating to qualified lessors) is amended by inserting "which is not a related person with respect to the lessee" before the comma at the end thereof.

(2) MAXIMUM LEASE TERM REDUCED.—Clause (iii) of section 168(f)(8)(B) (relating to term of lease) is amended to read as follows:

"(iii) the term of the lease (including any extensions) does not exceed the greater of—

"(I) 120 percent of the present class life of the property, or

"(II) the period equal to the recovery period determined with respect to such property under subsection (i)(2)."

(3) DEFINITION OF QUALIFIED LEASED PROPERTY.—Subparagraph (D) of section 168(f)(8) (defining qualified leased property) is amended to read as follows:

"(D) QUALIFIED LEASED PROPERTY DEFINED.—For purposes of this section—

"(i) IN GENERAL.—The term 'qualified leased property' means recovery property—

"(I) which is new section 38 property of the lessor, which is leased within 3 months after such property was placed in service, and which, if acquired by the lessee, would have been new section 38 property of the lessee, or

"(II) which was new section 38 property of the lessee, which is leased within 3 months after such property is placed in service by the lessee, and with respect to which the adjusted basis of the lessor does not exceed the adjusted basis of the lessee at the time of the lease.

"(ii) ONLY 45 PERCENT OF THE LESSEE'S PROPERTY MAY BE TREATED AS QUALIFIED.—The cost basis of all safe harbor lease property (determined without regard to this clause)—

"(I) which is placed in service during any calendar year, and

"(II) with respect to which the taxpayer is a lessee,

shall not exceed an amount equal to the 45 percent of the cost basis of the taxpayer's qualified base property placed in service during such calendar year.

"(iii) ALLOCATION OF DISQUALIFIED BASIS.—The cost basis not treated as qualified leased property under clause (ii) shall be allocated to safe harbor lease property for such calendar year (determined without regard to clause (ii)) in reverse order to when the agreement described in subparagraph (A) with respect to such property was entered into.

"(iv) CERTAIN PROPERTY MAY NOT BE TREATED AS QUALIFIED LEASED PROPERTY.—The term 'qualified leased property' shall not include recovery property—

"(I) which is a qualified rehabilitated building (within the meaning of section 48(g)(1)),

"(II) which is public utility property (within the meaning of section 167(l)(3)(A)),

"(III) which is property with respect to which a deduction is allowable by reason of section 291(b),

"(IV) with respect to which the lessee of the property (other than property described in clause (v)) under the agreement described in subparagraph (A) is a nonqualified tax-exempt organization, or

"(V) property with respect to which the user of such property is a person (other than a United States person) not subject to United States tax on income derived from the use of such property.

"(v) QUALIFIED MASS COMMUTING VEHICLES INCLUDED.—The term 'qualified leased property' includes recovery property which is a qualified mass commuting vehicle (as defined in section 103(b)(9)) which is financed in whole or in part by obligations the interest on which is excludable under section 103(a).

"(vi) QUALIFIED BASE PROPERTY.—For purposes of this subparagraph, the term 'qualified base property' means property placed in service during any calendar year which—

"(I) is new section 38 property of the taxpayer,

"(II) is safe harbor lease property (not described in subclause (I)) with respect to which the taxpayer is the lessee, or

"(III) is designated leased property (other than property described in subclause (I) or (II)) with respect which the taxpayer is the lessee.

Any designated leased property taken into account by any lessee under the preceding sentence shall not be taken into account by the lessor in determining the lessor's qualified base property. The lessor shall provide the lessee with such information with respect to the cost basis of such property as is necessary to carry out the purposes of this clause.

"(vii) DEFINITION OF DESIGNATED LEASED PROPERTY.—For purposes of this subparagraph, the term 'designated leased property' means property—

"(I) which is new section 38 property,

"(II) which is subject to a lease with respect to which the lessor of the property is treated (without regard to this paragraph) as the owner of the property for Federal tax purposes,

"(III) with respect to which the term of the lease to which such property is subject is more than 50 percent of the present class life (or, if no present class life, the recovery period used in subsection (i)(2)) of such property, and

"(IV) which the lessee designates on his return as designated leased property.

"(viii) DEFINITIONS; SPECIAL RULE.—For purposes of this subparagraph—

"(I) NEW SECTION 38 PROPERTY.—The term 'new section 38 property' has the meaning given such term by section 48(b).

"(II) PROPERTY PLACED IN SERVICE.—For purposes of this title (other than clause (i)), any property described in clause (i) to which subparagraph (A) applies shall be deemed originally placed in service not earlier than the date such property is used under the lease."

(4) DEFINITIONS AND SPECIAL RULES.—Paragraph (8) of section 168(f) (relating to special rules for leases) is amended by redesignating subparagraph (H) as subparagraph (K) and by inserting after subparagraph (G) the following new subparagraphs:

"(H) DEFINITIONS.—For purposes of this paragraph—

"(i) RELATED PERSON.—A person is related to another person if both persons are members of the same affiliated group (within the meaning of subsection (a) of section 1504 and determined without regard to subsection (b) of section 1504).

"(ii) NONQUALIFIED TAX-EXEMPT ORGANIZATION.—

"(I) IN GENERAL.—The term 'nonqualified tax-exempt organization' means, with respect to any agreement to which subparagraph (A) applies, any organization (or predecessor organization which was engaged in substantially similar activities) which was exempt from taxation under this title at any time during the 5-year period ending on the date such agreement was entered into.

"(II) SPECIAL RULE FOR FARMERS' COOPERATIVES.—The term 'nonqualified tax-exempt organization' shall not include any farmers' cooperative organization described in section 521 whether or not exempt from taxation under section 521.

"(III) SPECIAL RULE FOR PROPERTY USED IN UNRELATED TRADE OR BUSINESS.—An organization shall not be treated as a nonqualified tax-exempt organization with respect to any property if such property is used in an unrelated trade or business (within the meaning of section 513) of such organization which is subject to tax under section 511.

"(I) TRANSITIONAL RULES FOR CERTAIN TRANSACTIONS.—

"(i) IN GENERAL.—Except as provided in clause (ii), clause (ii) of subparagraph (D) shall not apply to any transitional safe harbor lease property (within the meaning of section 208(d)(3) of the Tax Equity and Fiscal Responsibility Act of 1982).

"(ii) SPECIAL RULES.—For purposes of subparagraph (D)(ii)—

"(I) DETERMINATION OF QUALIFIED BASE PROPERTY.—The cost basis of property described in clause (i) (and other property placed in service during 1982 to which subparagraph (D)(ii) does not apply) shall be taken into account in determining the qualified base property of the taxpayer for the taxable year in which such property was placed in service.

"(II) REDUCTION IN QUALIFIED LEASED PROPERTY.—The cost basis of property which may be treated as qualified leased property under subparagraph (D)(ii) for the taxable year in which such property was placed in service (determined without regard to this subparagraph) shall be reduced by the cost basis of the property taken into account under subclause (I).

"(J) COORDINATION WITH AT RISK RULES.—

"(i) IN GENERAL.—For purposes of section 465, in the case of property placed in service after the date of the enactment of this subparagraph, if—

"(I) an activity involves the leasing of section 1245 property which is safe harbor lease property, and

"(II) the lessee of such property (as determined under this paragraph) would, but for this paragraph, be treated as the owner of such property for purposes of this title,

then the lessor (as so determined) shall be considered to be at risk with respect to such property in an amount equal to the amount the lessee is considered at risk with respect to such property (determined under section 465 without regard to this paragraph).

"(ii) SUBPARAGRAPH NOT TO APPLY TO CERTAIN SERVICE CORPORATIONS.—Clause (i) shall not apply to any lessor which is a corporation the principal function of which is the performance of services in the field of health, law, engineering, architecture, accounting, actuarial science, performing arts, athletics, or consulting.

"(iii) SPECIAL RULE FOR PROPERTY PLACED IN SERVICE BEFORE DATE OF ENACTMENT OF THIS SUBPARAGRAPH.—This subparagraph shall apply to property placed in service before the date of enactment of this subparagraph if the provisions of section 465 did not apply to the lessor before such date but become applicable to such lessor after such date."

(c) CERTAIN LEASES BEFORE OCTOBER 20, 1981, TREATED AS QUALIFIED LEASES.—Nothing in paragraph (8) of section 168(f) of

the Internal Revenue Code of 1954, or in any regulations prescribed thereunder, shall be treated as making such paragraph inapplicable to any agreement entered into before October 20, 1981, solely because under such agreement 1 party to such agreement is entitled to the credit allowable under section 38 of such Code with respect to property and another party to such agreement is entitled to the deduction allowable under section 168 of such Code with respect to such property. Section 168(f)(8)(B)(ii) of such Code shall not apply to the party entitled to such credit.

(d) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by subsections (a) and (b) of this section shall apply to agreements entered into after July 1, 1982, or to property placed in service after July 1, 1982.

(2) TRANSITIONAL RULE FOR CERTAIN SAFE HARBOR LEASE PROPERTY.—

(A) IN GENERAL.—The amendments made by subsections (a) and (b) shall not apply to transitional safe harbor lease property.

(B) SPECIAL RULE FOR CERTAIN PROVISIONS.—Subparagraph (A) shall not apply with respect to the provisions of paragraph (6) of section 168(i) of the Internal Revenue Code of 1954 (as added by subsection (a)(1)), to the provisions of section 168(f)(8)(J) of such Code (as added by subsection (b)(4)), or to the amendment made by subsection (b)(1).

(3) TRANSITIONAL SAFE HARBOR LEASE PROPERTY.—For purposes of this subsection, the term "transitional safe harbor lease property" means property described in any of the following subparagraphs:

(A) IN GENERAL.—Property is described in this subparagraph if such property is placed in service before January 1, 1983, if—

(i) with respect to such property a binding contract to acquire or to construct such property was entered into by the lessee after December 31, 1980, and before July 2, 1982, or

(ii) such property was acquired by the lessee, or construction of such property was commenced by or for the lessee, after December 31, 1980, and before July 2, 1982.

(B) CERTAIN QUALIFIED LESSEES.—Property is described in this subparagraph if such property is placed in service before July 1, 1982, and with respect to which—

(i) an agreement to which section 168(f)(8)(A) of the Internal Revenue Code of 1954 applies was entered into before August 15, 1982, and

(ii) the lessee under such agreement is a qualified lessee (within the meaning of paragraph (6)).

(C) MANUFACTURERS OF CERTAIN PRODUCTS.—Property is described in this subparagraph if such property—

(i) is used to produce a class of products (within the meaning of paragraph (6)(B)) in an industry described in paragraph (6)(A)(ii)(II) (determined without regard to the phrase "other than the taxpayer"), and

(ii) would be described in subparagraph (A) if "October 1" were substituted for "January 1".

(D) Certain aircraft.—Property is described in this subparagaph if such property—

(i) is a commercial passenger aircraft (other than a helicopter), and

(ii) would be described in subparagraph (A) if "January 1, 1984" were substituted for "January 1, 1983".

For purposes of determining whether property described in this subparagraph is described in subparagraph (A), subparagraph (A)(ii) shall be applied by substituting "June 25, 1981" for "December 31, 1980" and by substituting "February 20, 1982" for "July 2, 1982" and construction of the aircraft shall be treated as having been begun during the period referred to in subparagraph (A)(ii) if during such period construction or reconstruction of a subassembly was commenced, or the stub wing join occurred.

(E) Turbines and boilers.—Property is described in this subparagraph if such property—

(i) is a turbine or boiler of a cooperative organization described in section 1381(a), and

(ii) would be property described in subparagraph (A) if "July 1" were substituted for "January 1".

For purposes of determining whether property described in this subparagraph is described in subparagraph (A), such property shall be treated as having been acquired during the period referred to in subparagraph (A)(ii) if at least 20 percent of the cost of such, property is paid during such period.

(F) Property used in the production of steel.—Property is described in this subparagraph if such property—

(i) is used by the taxpayer directly in connection with the trade or business of the taxpayer of the manufacture or production of steel, and

(ii) would be described in subparagraph (A) if "January 1, 1984" were substituted for "January 1, 1983".

(4) Special rule for antiavoidance provisions.—The provisions of paragraph (6) of section 168(i) of such Code (as added by subsection (a)(1)), and the amendment made by subsection (b)(1), shall apply to leases entered into after February 19, 1982, in taxable years ending after such date.

(5) Special rule for mass commuting vehicles.—The amendments made by this section (other than section 168(i) (1) and (7) of such Code, as added by subsection (a)(1)) and section 209 shall not apply to qualified leased property described in section 168(f)(8)(D)(V) of such Code (as in effect after the amendments made by this section) which—

(A) is placed in service before January 1, 1988, or

(B) is placed in service after such date—

(i) pursuant to a binding contract or commitment entered into before April 1, 1983, and

(ii) solely because of conditions which, as determined by the Secretary of the Treasury or his delegate, are not within the control of the lessor or lessee.

(6) Qualified lessee defined.—

(A) In general.—The term "qualified lessee" means a taxpayer which is a lessee of an agreement to which section 168(f)(8)(A) of such Code applies and which—

(i) had net operating losses in each of the three most recent taxable years ending before July 1, 1982, and had an aggregate net operating loss for the five most recent taxable years ending before July 1, 1982, and

(ii) which uses the property subject to the agreement to manufacture and produce within the United States a class of products in an industry with respect to which—

(I) the taxpayer produced less than 5 percent of the total number of units (or value) of such products during the period covering the three most recent taxable years of the taxpayer ending before July 1, 1982, and

(II) four or fewer United States persons (including as one person an affiliated group as defined in section 1504(a)) other than the taxpayer manufactured 85 percent or more of the total number of all units (or value) within such class of products manufactured and produced in the United States during such period.

(B) Class of products.—For purposes of subparagraph (A)—

(i) the term "class of products" means any of the categories designated and numbered as a "class of products" in the 1977 Census of Manufacturers compiled and published by the Secretary of Commerce under title 13 of the United States Code, and

(ii) information—

(I) compiled or published by the Secretary of Commerce, as part of or in connection with the Statistical Abstract of the United States or the Census of Manufacturers, regarding the number of units (or value) of a class of products manufactured and produced in the United States during any period, or

(II) if information under subclause (I) is not available, so compiled or published with respect to the number of such units shipped or sold by such manufacturers during any period,

shall constitute prima facie evidence of the total number of all units of such class of products manufactured and produced in the United States in such period.

(6) Underpayments of tax for 1982.—No addition to the tax shall be made under section 6655 of the Internal Revenue Code of 1954 (relating to failure by corporation to pay estimated income tax) for any period before October 15, 1982, with respect to any underpayment of estimated tax by a taxpayer with respect to any tax imposed by chapter 1 of such Code, to the

extent that such underpayment was created or increased by any provision of this section.

SEC. 209. REPEAL OF LEASING; SPECIAL RULE FOR LEASES WITH ECONOMIC SUBSTANCE.

(a) SPECIAL RULE FOR LEASES WITH ECONOMIC SUBSTANCE.—Paragraph (8) of section 168(f) (relating to special rules for leasing) is amended to read as follows:

"(8) SPECIAL RULES FOR FINANCE LEASES.—

"(A) IN GENERAL.—For purposes of this title, except as provided in subsection (i), in the case of any agreement with respect to any finance lease property, the fact that—

"(i) a lessee has the right to purchase the property at a fixed price which is not less than 10 percent of the original cost of the property to the lessor, or

"(ii) the property is of a type not readily usable by any person other than the lessee,

shall not be taken into account in determining whether such agreement is a lease.

"(B) FINANCE LEASE PROPERTY DEFINED.—For purposes of this section—

"(i) IN GENERAL.—The term 'finance lease property' means recovery property which is subject to an agreement which meets the requirements of subparagraph (C) and—

"(I) which is new section 38 property of the lessor, which is leased within 3 months after such property was placed in service, and which, if acquired by the lessee, would have been new section 38 property of the lessee, or

"(II) which was new section 38 property of the lessee, which is leased within 3 months after such property is placed in service by the lessee, and with respect to which the adjusted basis of the lessor does not exceed the adjusted basis of the lessee at the time of the lease.

"(ii) ONLY 40 PERCENT OF THE LESSEE'S PROPERTY MAY BE TREATED AS QUALIFIED.—The cost basis of all finance lease property (determined without regard to this clause)—

"(I) which is placed in service during any calendar year beginning before January 1, 1986, and

"(II) with respect to which the taxpayer is a lessee,

shall not exceed an amount equal to 40 percent of the cost basis of the taxpayer's qualified base property placed in service during such calendar year.

"(iii) ALLOCATION OF DISQUALIFIED BASIS.—The cost basis not treated as finance lease property under clause (ii) shall be allocated to finance lease property for such calendar year (determined without regard to clause (ii)) in reverse order to when the agreement described in subparagraph (A) with respect to such property was entered into.

"(iv) CERTAIN PROPERTY MAY NOT BE TREATED AS FINANCE LEASE PROPERTY.—The term 'finance lease property' shall not include recovery property—

"(I) which is a qualified rehabilitated building (within the meaning of section 48(g)(1)),

"(II) which is public utility property (within the meaning of section 167(l)(3)(A)),

"(III) which is property with respect to which a deduction is allowable by reason of section 291(b),

"(IV) with respect to which the lessee of the property under the agreement described in subparagraph (A) is a nonqualified tax-exempt organization, or

"(V) property with respect to which the user of such property is a person (other than a United States person) not subject to United States tax on income derived from the use of such property.

"(v) QUALIFIED BASE PROPERTY.—For purposes of this subparagraph, the term 'qualified base property' means property placed in service during any calendar year which—

"(I) is new section 38 property of the taxpayer,

"(II) is finance lease property (not described in subclause (I)) with respect to which the taxpayer is the lessee, or

"(III) is designated leased property (other than property described in subclause (I) or (II)) with respect to which the taxpayer is the lessee.

Any designated leased property taken into account by any lessee under the preceding sentence shall not be taken into account by the lessor in determining the lessor's qualfied base property. The lessor shall provide the lessee with such information with respect to the cost basis of such property as is necessary to carry out the purposes of this clause.

"(vi) DEFINITION OF DESIGNATED LEASED PROPERTY.—For purposes of this subparagraph, the term 'designated leased property' means property—

"(I) which is new section 38 property,

"(II) which is subject to a lease with respect to which the lessor of the property is treated (without regard to this paragraph) as the owner of the property for Federal tax purposes,

"(III) with respect to which the term of the lease to which such property is subject is more than 50 percent of the present class life (or, if no present class life, the recovery period under subsection (a)) of such property, and

"(IV) which the lessee designates on his return as designated leased property.

"(vii) DEFINITION; SPECIAL RULES.—For purposes of this subparagraph—

"(I) New section 38 property defined.—The term 'new section 38 property' has the meaning given such term by section 48(b).

"(II) Lessee limitation not to apply to certain farm property.—Clause (ii) shall not apply to any property which is used for farming purposes (within the meaning of section 2032A(e)(5)) and which is placed in service during the taxable year but only if the cost basis of such property, when added to the cost basis of other finance lease property used for such purpose does not exceed $150,000 (determined under rules similar to the rules of section 209(d)(1)(B) of the Tax Equity and Fiscal Responsibility Act of 1982).

"(III) Property placed in service.—For purposes of this title (other than clause (i), any finance lease property shall be deemed originally placed in service not earlier than the date such property is used under the lease.

"(C) Agreements must meet certain requirements.—The requirements of this subparagraph are met with respect to any agreement if—

"(i) Lessor requirement.—Any lessor under the agreement must be—

"(I) a corporation (other than an electing small business corporation within the meaning of section 1371(b) or a personal holding company within the meaning of section 542(a)),

"(II) a partnership all of the partners of which are corporations described in subclause (I), or

"(III) a grantor trust with respect to which the grantor and all the beneficiaries of the trust are described in subclause (I) or (II).

"(ii) Characterization of agreement.—The parties to the agreement characterize such agreement as a lease.

"(iii) Agreement contains certain provisions.—The agreement contains the provision described in clause (i) or (ii) of subparagraph (A), or both.

"(iv) For purposes of this title (determined without regard to the provisions described in clause (iii)), the agreement would be treated as a lease and the lessor under the agreement would be treated as the owner of the property.

"(D) Paragraph not to apply to agreements between related persons.—This paragraph shall not apply to any agreement if the lessor and lessee are both persons who are members of the same affiliated group (within the meaning of subsection (a) of section 1504 and determined without regard to subsection (b) of section 1504).

"(E) Nonqualified tax-exempt organization.—

"(i) In general.—The term 'nonqualified tax-exempt organization' means, with respect to any agreement to which subparagraph (A) applies, any organization (or

predecessor organization which was engaged in substantially similar activities) which was exempt from taxation under this title at any time during the 5-year period ending on the date such agreement was entered into.

"(ii) SPECIAL RULE FOR FARMERS' COOPERATIVES.—The term 'nonqualified tax-exempt organization' shall not include any farmers' cooperative organization which is described in section 521 whether or not exempt from taxation under section 521.

"(iii) SPECIAL RULE FOR PROPERTY USED IN UNRELATED TRADE OR BUSINESS.—An organization shall not be treated as a nonqualified tax-exempt organization with respect to any property if such property is used in an unrelated trade or business (within the meaning of section 513) of such organization which is subject to taxation under section 511.

"(F) CROSS REFERENCE.—

"For special recapture in case where lessee acquires financed recovery property, see section 1245."

(b) SPECIAL LIMITATIONS ON FINANCE LEASE PROPERTY.—Subsection (i) of section 168 (relating to limitations and additional requirements with respect to leases) is amended to read as follows:

"(i) LIMITATIONS RELATING TO LEASES OF FINANCE LEASE PROPERTY.—For purposes of this subtitle, in the case of finance lease property, the following limitations shall apply:

"(1) LESSOR MAY NOT REDUCE TAX LIABILITY BY MORE THAN 50 PERCENT.—

"(A) IN GENERAL.—The aggregate amount allowable as deductions or credits for any taxable year which are allocable to all finance lease property with respect to which the taxpayer is the lessor may not reduce the liability for tax of the taxpayer for such taxable year (determined without regard to finance lease items) by more than 50 percent of such liability.

"(B) CARRYOVER OF AMOUNTS NOT ALLOWABLE AS DEDUCTIONS OR CREDITS.—Any amount not allowable as a deduction or credit under subparagraph (A)—

"(i) may be carried over to any subsequent taxable year, and

"(ii) shall be treated as a deduction or credit allocable to finance lease property in such subsequent taxable year.

"(C) ALLOCATION AMONG DEDUCTIONS AND CREDITS.—The Secretary shall prescribe regulations for determining the amount—

"(i) of any deduction or credit allocable to finance lease property for any taxable year to which subparagraph (A) applies, and

"(ii) of any carryover of any such deduction or credit under subparagraph (B) to any subsequent taxable year.

"(D) LIABILITY FOR TAX AND FINANCE LEASE ITEMS DEFINED.—For purposes of this paragraph—

"(i) LIABILITY FOR TAX DEFINED.—Except as provided in this subparagraph, the term 'liability for tax' means the tax imposed by this chapter, reduced by the sum of the credits allowable under subpart A of part IV of subchapter A of this chapter.

"(ii) FINANCE LEASE ITEMS DEFINED.—The term 'finance lease items' means any of the following items which are properly allocable to finance lease property with respect to which the taxpayer is the lessor:

"(I) Any deduction or credit allowable under this chapter (other than any deduction for interest).

"(II) Any rental income received by the taxpayer from any lessee of such property.

"(III) Any interest allowable as a deduction under this chapter on indebtedness of the taxpayer (or any related person within the meaning of subsection (e)(4)(D)) which is paid or incurred to the lessee of such property (or any person so related to the lessee).

"(iii) CERTAIN TAXES NOT INCLUDED.—The term 'tax imposed by this chapter' shall not include any tax treated as not imposed by this chapter under the last sentence of section 53(a) (other than the tax imposed by section 56).

"(E) CERTAIN SAFE HARBOR LEASE PROPERTY TAKEN INTO ACCOUNT.—Under regulations prescribed by the Secretary, deductions and credits and safe harbor lease items which are allocable to safe harbor lease property to which this paragraph (as in effect for taxable years beginning in 1983) applies shall be taken into account for purposes of applying this paragraph.

"(2) INVESTMENT CREDIT ALLOWED ONLY OVER 5-YEAR PERIOD.—In the case of any credit which would otherwise be allowable under section 38 with respect to any finance lease property for any taxable year (determined without regard to this paragraph), only 20 percent of the amount of such credit shall be allowable in such taxable year and 20 percent of such amount shall be allowable in each of the succeeding 4 taxable years.

"(3) COMPUTATION OF TAXABLE INCOME OF LESSEE FOR PURPOSES OF PERCENTAGE DEPLETION.—

"(A) IN GENERAL.—For purposes of section 613 or 613A, the taxable income of any taxpayer who is a lessee of any financed recovery property shall be computed as if the taxpayer was the owner of such property, except that the amount of the deduction under subsection (a) of this section shall be determined after application of paragraph (2) of this subsection.

"(B) Coordination with crude oil windfall profit tax.—Section 4988(b)(3)(A) shall be applied without regard to subparagraph (A).

"(4) LIMITATIONS.—

"(A) TERMINATION OF CERTAIN PROVISIONS.—

"(i) PARAGRAPH (1).—Paragraph (1) shall not apply to property placed in service after September 30, 1985, in taxable years beginning after such date.

"(ii) PARAGRAPH (2).—Paragraph (2) shall not apply to property placed in service after September 30, 1985.

"(B) CERTAIN FARM PROPERTY.—This subsection shall not apply to property which is used for farming purposes (within the meaning of section 2032A(e)(5)) and which is placed in service during the taxable year but only if the cost basis of such property, when added to the cost basis of other finance lease property used for such purpose, does not exceed $150,000 (determined under rules similar to the rules of section 209(d)(1)(B) of the Tax Equity and Fiscal Responsibility Act of 1982)."

(c) DEFINITION OF NEW SECTION 38 PROPERTY.—Subsection (b) of section 48 (defining new section 38 property) is amended by adding at the end thereof the following new sentence: "For purposes of determining whether section 38 property subject to a lease is new section 38 property, such property shall be treated as originally placed in service not earlier than the date such property is used under the lease but only if such property is leased within 3 months after such property is placed in service."

(d) EFFECTIVE DATES.—

(1) SUBSECTION (a).—

(A) IN GENERAL.—Except as provided in subparagraph (B) and paragraph (2), the amendments made by this section shall apply to agreements entered into after December 31, 1983.

(B) SPECIAL RULE FOR FARM PROPERTY AGGREGATING $150,000 OR LESS.—

(i) IN GENERAL.—The amendments made by subsection (a) shall also apply to any agreement entered into after July 1, 1982, and before January 1, 1984, if the property subject to such agreement is section 38 property which is used for farming purposes (within the meaning of section 2032A(e)(5)).

(ii) $150,000 LIMITATION.—The provisions of clause (i) shall not apply to any agreement if the sum of—

(I) the cost basis of the property subject to the agreement, plus

(II) the cost basis of any property subject to an agreement to which this subparagraph previously applied, which was entered into during the same calendar year, and with respect to which the lessee was the lessee of the agreement described in subclause (I) (or any related person within the meaning of section 168(e)(4)(D)),

exceeds $150,000. For purposes of subclause (II), in the case of an individual, there shall not be taken into account any agreement of any individual who is a related person involving property which is used in a trade or business of farming of such related person which is separate from the trade or business of farming of the lessee described in subclause (II).

(2) SPECIAL RULE FOR DEFINITION OF NEW SECTION 38 PROPERTY.—The amendment made by subsection (c) shall apply to property placed in service after December 31, 1983.

SEC. 210. MOTOR VEHICLE OPERATING LEASES.

(a) IN GENERAL.—In the case of any qualified motor vehicle agreement, the fact that such agreement contains a terminal rental adjustment clause shall not be taken into account in determining whether such agreement is a lease.

(b) DEFINITIONS.—For purposes of this section—

(1) QUALIFIED MOTOR VEHICLE AGREEMENT.—The term "qualified motor vehicle agreement" means any agreement with respect to a motor vehicle (including a trailer)—

(A) which was entered into before—

(i) the enactment of any law, or

(ii) the publication by the Secretary of the Treasury or his delegate of any regulation,

which provides that any agreement with a terminal rental adjustment clause is not a lease,

(B) with respect to which the lessor under the agreement—

(i) is personally liable for the repayment of, or

(ii) has pledged property (but only to the extent of the net fair market value of the lessor's interest in such property), other than property subject to the agreement or property directly or indirectly financed by indebtedness secured by property subject to the agreement, as security for,

all amounts borrowed to finance the acquisition of property subject to the agreement, and

(C) with respect to which the lessee under the agreement uses the property subject to the agreement in a trade or business or for the production of income.

(2) TERMINAL RENTAL ADJUSTMENT CLAUSE.—The term "terminal rental adjustment clause" means a provision of an agreement which permits or requires the rental price to be adjusted upward or downward by reference to the amount realized by the lessor under the agreement upon sale or other disposition of such property.

PART III—FOREIGN TAX

SEC. 211. FOREIGN TAX CREDIT FOR TAXES ON OIL AND GAS INCOME.

(a) AMENDMENT OF SECTION 907(c)(4) TO RECAPTURE FOREIGN OIL AND GAS EXTRACTION LOSSES BY RECHARACTERIZING LATER EXTRACTION INCOME.—Paragraph (4) of section 907(c) (relating to certain losses) is amended to read as follows:

"(4) RECAPTURE OF FOREIGN OIL AND GAS EXTRACTION LOSSES BY RECHARACTERIZING LATER EXTRACTION INCOME.—

"(A) IN GENERAL.—That portion of the income of the taxpayer for the taxable year which (but for this paragraph) would be treated as foreign oil and gas extraction income shall be treated as income (from sources without the United States) which is not foreign oil and gas extraction income to the extent of the excess of—

"(i) the aggregate amount of foreign oil extraction losses for preceding taxable years beginning after December 31, 1982, over

"(ii) so much of such aggregate amount as was recharacterized under this subparagraph for preceding taxable years beginning after December 31, 1982.

"(B) FOREIGN OIL EXTRACTION LOSS DEFINED.—

"(i) IN GENERAL.—For purposes of this paragraph, the term 'foreign oil extraction loss' means the amount by which—

"(I) the gross income for the taxable year from sources without the United States and its possessions (whether or not the taxpayer chooses the benefits of this subpart for such taxable year) taken into account in determining the foreign oil and gas extraction income for such year, is exceeded by

"(II) the sum of the deductions properly apportioned or allocated thereto.

"(ii) NET OPERATING LOSS DEDUCTION NOT TAKEN INTO ACCOUNT.—For purposes of clause (i), the net operating loss deduction allowable for the taxable year under section 172(a) shall not be taken into account.

"(iii) EXPROPRIATION AND CASUALTY LOSSES NOT TAKEN INTO ACCOUNT.—For purposes of clause (i), there shall not be taken into account—

"(I) any foreign expropriation loss (as defined in section 172(h)) for the taxable year, or

"(II) any loss for the taxable year which arises from fire, storm, shipwreck, or other casualty, or from theft,

to the extent such loss is not compensated for by insurance or otherwise."

(b) EXTRACTION INCOME REMOVED FROM FOREIGN OIL RELATED INCOME.—Paragraph (2) of section 907(c) (defining foreign oil related income) is amended to read as follows:

"(2) FOREIGN OIL RELATED INCOME.—The term 'foreign oil related income' means the taxable income derived from sources outside the United States and its possessions from—

"(A) the processing of minerals extracted (by the taxpayer or by any other person) from oil or gas wells into their primary products,

"(B) the transportation of such minerals or primary products,

"(C) the distribution or sale of such minerals or primary products,

"(D) the disposition of assets used by the taxpayer in the trade or business described in subparagraph (A), (B), or (C), or

"(E) the performance of any other related service."

(c) REPEAL OF SEPARATE APPLICATION OF SECTION 904 TO FOREIGN OIL RELATED INCOME; AMOUNTS TREATED AS FOREIGN TAXES ON SUCH INCOME.—

(1) IN GENERAL.—Subsection (b) of section 907 (relating to special rules in case of foreign oil and gas income) is amended to read as follows:

"(b) FOREIGN TAXES ON FOREIGN OIL RELATED INCOME.—For purposes of this subtitle, in the case of taxes paid or accrued to any foreign country with respect to foreign oil related income, the term 'income, war profits, and excess profits taxes' shall not include any amount paid or accrued after December 31, 1982, to the extent that the Secretary determines that the foreign law imposing such amount of tax is structured, or in fact operates, so that the amount of tax imposed with respect to foreign oil related income will generally be materially greater, over a reasonable period of time, than the amount generally imposed on income that is neither foreign oil related income nor foreign oil and gas extraction income. In computing the amount not treated as tax under this subsection, such amount shall be treated as a deduction under the foreign law."

(2) REPEAL OF SEPARATE TREATMENT OF FOREIGN OIL RELATED LOSS.—Subsection (f) of section 904 (relating to recapture of overall foreign loss) is amended by striking out paragraph (4) and redesignating paragraphs (5) and (6) as paragraphs (4) and (5), respectively.

(d) CARRYBACK AND CARRYOVER OF DISALLOWED CREDITS; TRANSITIONAL RULES.—

(1) TRANSITIONAL RULES.—Subsection (e) of section 907 (relating to transitional rules) is amended to read as follows:

"(e) TRANSITIONAL RULES.—

"(1) CREDITS ARISING IN TAXABLE YEARS BEGINNING BEFORE JANUARY 1, 1983.—The amount of taxes paid or accrued in any taxable year beginning before January 1, 1983 (hereinafter in this paragraph referred to as the 'excess credit year') which under section 904(c) or 907(f) may be deemed paid or accrued in a taxable year beginning after December 31, 1982, shall not

exceed the amount which could have been deemed paid or accrued if sections 907(b), 907(f), and 904(f)(4) (as in effect on the day before the date of the enactment of the Tax Equity and Fiscal Responsibility Act of 1982) remained in effect for taxable years beginning after December 31, 1982.

"(2) CARRYBACK OF CREDITS ARISING IN TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1982.—The amount of the taxes paid or accrued in a taxable year beginning after December 31, 1982, which may be deemed paid or accrued under section 904(c) or 907(f) in a taxable year beginning before January 1, 1983, shall not exceed the amount which could have been deemed paid or accrued if sections 907(b), 907(f), and 904(f)(4) (as in effect on the day before the date of the enactment of the Tax Equity and Fiscal Responsibility Act of 1982) remained in effect for taxable years beginning after December 31, 1982."

(2) REPEAL OF 2-PERCENT LIMITATION ON CARRYBACK AND CARRYOVER OF DISALLOWED EXTRACTION TAXES.—

(A) IN GENERAL.—Paragraph (1) of section 907(f) (relating to carryback and carryover of disallowed credits) is amended—

(i) by striking out "so much of such excess as does not exceed 2 percent of foreign oil and gas extraction income for such taxable year" and inserting in lieu thereof "such excess",

(ii) by striking out the last sentence.

(B) TECHNICAL AMENDMENTS.—

(i) Subparagraph (B) of section 907(f)(2) is amended—

(I) by striking out "on taxes paid or accrued with respect to foreign oil related income", and

(II) by striking out "with respect to such income" in clause (i).

(ii) Subparagraph (A) of section 907(f)(3) is amended by striking out "with respect to oil-related income".

(iii) Subparagraph (B) of section 907(f)(3) is amended by striking out "oil-related".

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1982.

(2) RETENTION OF OLD SECTIONS 907(b) AND 904(f)(4) WHERE TAXPAYER HAD FOREIGN LOSS FROM AN ACTIVITY NOT RELATED TO OIL AND GAS.—If, after applying old sections 907(b) and 904(f)(4) to a taxable year beginning before January 1, 1983, the taxpayer had a foreign loss attributable to activities not taken into account in determining foreign oil related income (as defined in old section 907(c)(2)), such loss shall not be recaptured from foreign oil related income more rapidly than ratably over the 8-year period beginning with the first taxable year beginning after December 31, 1982. For purposes of the preceding sentence, an "old" section is such section as in effect on the day before the date of the enactment of this Act.

SEC. 212. CURRENT TAXATION OF FOREIGN OIL RELATED INCOME OF CONTROLLED FOREIGN CORPORATIONS.

(a) FOREIGN OIL RELATED INCOME ADDED TO CURRENTLY TAXED AMOUNTS.—Subsection (a) of section 954 (defining foreign base company income) is amended by adding at the end thereof the following new paragraph:

"(5) the foreign base company oil related income for the taxable year (determined under subsection (h) and reduced as provided in subsection (b)(5))."

(b) SPECIAL RULES.—

(1) ALLOWANCE OF DEDUCTIONS AGAINST FOREIGN BASE COMPANY OIL RELATED INCOME.—Paragraph (5) of section 954(b) is amended by striking out "and the foreign base company shipping income" and inserting in lieu thereof ", the foreign base company shipping income, and the foreign base company oil related income".

(2) PREEMPTION OF FOREIGN BASE COMPANY OIL RELATED INCOME.—Subsection (b) of section 954 is amended by adding at the end thereof the following new paragraph:

"(8) FOREIGN BASE COMPANY OIL RELATED INCOME NOT TREATED AS ANOTHER KIND OF BASE COMPANY INCOME.—Income of a corporation which is foreign base company oil related income shall not be considered foreign base company income of such corporation under paragraph (1), (2), or (3) of subsection (a)."

(c) DEFINITION OF FOREIGN BASE COMPANY OIL RELATED INCOME.—Section 954 (relating to foreign base company income) is amended by adding at the end thereof the following new subsection:

"(h) FOREIGN BASE COMPANY OIL RELATED INCOME.—For purposes of this section—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, the term 'foreign base company oil related income' means foreign oil related income (within the meaning of section 907(c)(2)) other than income derived from a source within a foreign country in connection with—

"(A) oil or gas which was extracted from an oil or gas well located in such foreign country, or

"(B) oil, gas, or a primary product of oil or gas which is sold by the foreign corporation or a related person for use or consumption within such country or is loaded in such country on a vessel or aircraft as fuel for such vessel or aircraft.

"(2) PARAGRAPH (1) APPLIES ONLY WHERE CORPORATION HAS PRODUCED 1,000 BARRELS PER DAY OR MORE.—

"(A) IN GENERAL.—The term 'foreign base company oil related income' shall not include any income of a foreign corporation if such corporation is not a large oil producer for the taxable year.

"(B) LARGE OIL PRODUCER.—For purposes of subparagraph (A), the term 'large oil producer' means any corporation if, for the taxable year or for any preceding taxable year, the average daily production of foreign crude oil and natural gas of the related group which includes such corporation equaled or exceeded 1,000 barrels.

"(C) Related group.—The term 'related group' means a group consisting of the foreign corporation and any other person who is a related person with respect to such corporation.

"(D) Average daily production of foreign crude oil and natural gas.—For purposes of this paragraph, the average daily production of foreign crude oil or natural gas of any related group for any taxable year (and the conversion of cubic feet of natural gas into barrels) shall be determined under rules similar to the rules of section 613A except that only crude oil or natural gas from a well located outside the United States shall be taken into account."

(d) Exception From Foreign Base Company Income for Certain Foreign Corporations Not To Apply.—Paragraph (4) of section 954(b) is amended by adding at the end thereof the following new sentence: "The preceding sentence shall not apply to foreign base company oil related income described in subsection (a)(5)."

(e) Conforming Amendments.—Subsection (a) of section 954 is amended by striking out "and" at the end of paragraph (3), and by striking out the period at the end of paragraph (4) and inserting in lieu thereof", and".

(f) Effective Date.—The amendments made by this section shall apply to taxable years of foreign corporations beginning after December 31, 1982, and to taxable years of United States shareholders in which, or with which, such taxable years of foreign corporations end.

SEC. 213. POSSESSION TAX CREDIT; INCOME TAX LIABILITY INCURRED TO THE VIRGIN ISLANDS.

(a) Possession Tax Credit.—

(1) Active trade or business requirement.—Paragraph (2) of section 936(a) (relating to conditions which must be satisfied) is amended—

(A) by striking out "50 percent" in subparagraph (B) and inserting in lieu thereof "65 percent", and

(B) by adding at the end thereof the following new subparagraph:

"(C) Transitional rule.—In applying subparagraph (B) with respect to taxable years beginning after December 31, 1982, and before January 1, 1985, the following percentage shall be substituted for "65 percent":

"For taxable years beginning in calendar year:	*The percentage tax is:*
1983	*55*
1984	*60".*

(2) Income attributable to certain intangible property.—Section 936 (relating to Puerto Rico and possession tax credit) is amended by adding at the end thereof the following new subsection:

"(h) Tax Treatment of Intangible Property Income.—

"(1) In general.—

"(A) Income attributable to shareholders.—The intangible property income of a corporation electing the application of this section for any taxable year shall be included

on a pro rata basis in the gross income of all shareholders of such electing corporation at the close of the taxable year of such electing corporation as income from sources within the United States for the taxable year of such shareholder in which or with which the taxable year of such electing corporation ends.

"(B) EXCLUSION FROM THE INCOME OF AN ELECTING CORPORATION.—Any intangible property income of a corporation electing the application of this section which is included in the gross income of a shareholder of such corporation by reason of subparagraph (A) shall be excluded from the gross income of such corporation.

"(2) FOREIGN SHAREHOLDERS; SHAREHOLDERS NOT SUBJECT TO TAX.—

"(A) IN GENERAL.—Paragraph (1)(A) shall not apply with respect to any shareholder—

"(i) who is not a United States person, or

"(ii) who is not subject to tax under this title on intangible property income which would be allocated to such shareholder (but for this subparagraph).

"(B) TREATMENT OF NONALLOCATED INTANGIBLE PROPERTY INCOME.—For purposes of this subtitle, intangible property income of a corporation electing the application of this section which is not included in the gross income of a shareholder of such corporation by reason of subparagraph (A)—

"(i) shall be treated as income from sources within the United States, and

"(ii) shall not be taken into account under subsection (a)(2).

"(3) INTANGIBLE PROPERTY INCOME.—For purposes of this subsection—

"(A) IN GENERAL.—The term 'intangible property income' means the gross income of a corporation attributable to any intangible property other than intangible property which has been licensed to such corporation since prior to 1948 and is in use by such corporation on the date of the enactment of this subparagraph.

"(B) INTANGIBLE PROPERTY.—The term 'intangible property' means any—

"(i) patent, invention, formula, process, design, pattern, or know-how;

"(ii) copyright, literary, musical, or artistic composition;

"(iii) trademark, trade name, or brand name;

"(iv) franchise, license, or contract;

"(v) method, program, system, procedure, campaign, survey, study, forecast, estimate, customer list, or technical data; or

"(vi) any similar item,

which has substantial value independent of the services of any individual.

"(C) EXCLUSION OF REASONABLE PROFIT.—The term 'intangible property income' shall not include any portion of *the income from the sale, exchange or other disposition of any product, or from the rendering of services, by a corporation electing the application of this section which is determined by the Secretary to be a reasonable profit on the direct and indirect costs incurred by such electing corporation which are attributable to such income.*

"(D) RELATED PERSON.—

"(i) IN GENERAL.—A person (hereinafter referred to as the 'related person') is related to any person if—

"(I) the related person bears a relationship to such person specified in section 267(b) or section 707(b)(1), or

"(II) the related person and such person are members of the same controlled group of corporations.

"(ii) SPECIAL RULES.—For purposes of clause (i)—

"(I) section 267(b) and section 707(b)(1) shall be applied by substituting '10 percent' for '50 percent', and

"(II) section 267(b)(3) shall be applied without regard to whether a person was a personal holding company or a foreign personal holding company.

"(E) CONTROLLED GROUP OF CORPORATIONS.—The term 'controlled group of corporations' has the meaning given to such term by section 1563(a), except that—

"(i) 'more than 10 percent' shall be substituted for 'at least 80 percent' and 'more than 50 percent' each place either appears in section 1563(a), and

"(ii) the determination shall be made without regard to subsections (a)(4), (b)(2), and (e)(3)(C) of section 1563.

"(4) DISTRIBUTIONS TO MEET QUALIFICATION REQUIREMENTS.—

"(A) IN GENERAL.—If the Secretary determines that a corporation does not satisfy a condition specified in subparagraph (A) or (B) of subsection (a)(2) for any taxable year by reason of the exclusion from gross income under paragraph (1)(B), such corporation shall nevertheless be treated as satisfying such condition for such year if it makes a pro rata distribution of property after the close of such taxable year to its shareholders (designated at the time of such distribution as a distribution to meet qualification requirements) with respect to their stock in an amount which is equal to—

"(i) if the condition of subsection (a)(2)(A) is not satisfied, that portion of the gross income for the period described in subsection (a)(2)(A)—

"(I) which was not derived from sources within a possession, and

"(II) which exceeds the amount of such income for such period which would enable such corporation to satisfy the condition of subsection (a)(2)(A),

"(ii) if the condition of subsection (a)(2)(B) is not satisfied, that portion of the gross income for such period—

"(I) which was not derived from the active conduct of a trade or business within a possession, and

"(II) which exceeds the amount of such income for such period which would enable such corporation to satisfy the conditions of subsection (a)(2)(B), or

"(iii) if neither of such conditions is satisfied, that portion of the gross income which exceeds the amount of gross income for such period which would enable such corporation to satisfy the conditions of subparagraphs (A) and (B) of subsection (a)(2).

"(B) EFFECTIVELY CONNECTED INCOME.—In the case of a shareholder who is a nonresident alien individual or a foreign corporation, trust, or estate, any distribution described in subparagraph (A) shall be treated as income which is effectively connected with the conduct of a trade or business conducted through a permanent establishment of such shareholder within the United States.

"(C) DISTRIBUTION DENIED IN CASE OF FRAUD OR WILLFUL NEGLECT.—Subparagraph (A) shall not apply to a corporation if the determination of the Secretary described in subparagraph (A) contains a finding that the failure of such corporation to satisfy the conditions in subsection (a)(2) was due in whole or in part to fraud with intent to evade tax or willful neglect on the part of such corporation.

"(5) ELECTION OUT.—

"(A) IN GENERAL.—The rules contained in paragraphs (1) through (4) do not apply for any taxable year if an election pursuant to subparagraph (F) is in effect to use one of the methods specified in subparagraph (C).

"(B) ELIGIBILITY.—

"(i) REQUIREMENT OF SIGNIFICANT BUSINESS PRESENCE.—An election may be made to use one of the methods specified in subparagraph (C) with respect to a product or type of service only if an electing corporation has a significant business presence in a possession with respect to such product or type of service. An election may remain in effect with respect to such product or type of service for any subsequent taxable year only if such electing corporation maintains a significant business presence in a possession with respect to such product or type of service in such subsequent taxable year. If an election is not in effect for a taxable year because of the preceding sentence, the electing corporation shall be deemed to have revoked the election on the first day of such taxable year.

"(ii) DEFINITION.—For purposes of this subparagraph, an electing corporation has a 'significant business presence' in a posession for a taxable year with respect to a product or type of service if:

"(I) the total production costs (other than direct material costs and other than interest excluded by regulations prescribed by the Secretary) incurred by *the electing corporation in the possession in producing units of that product sold or otherwise disposed of during the taxable year by the affiliated group to persons who are not members of the affiliated group are not less than 25 percent of the difference between (a) the gross receipts from sales or other dispositions during the taxable year by the affiliated group to persons who are not members of the affiliated group of such units of the product produced, in whole or in part, by the electing corporation in the possession, and (b) the direct material costs of the purchase of materials for such units of that product by all members of the affiliated group from persons who are not members of the affiliated group; or*

"(II) no less than 65 percent of the direct labor costs of the affiliated group for units of the product produced during the taxable year in whole or in part by the electing corporation or for the type of service rendered by the electing corporation during the taxable year, is incurred by the electing corporation and is compensation for services performed in the possession; or

"(III) with respect to purchases and sales by an electing corporation of all goods not produced in whole or in part by any member of the affiliated group and sold by the electing corporation to persons other than members of the affiliated group, no less than 65 percent of the total direct labor costs of the affiliated group in connection with all purchases and sales of such goods sold during the taxable year by such electing corporation is incurred by such electing corporation and is compensation for services performed in the possession.

Notwithstanding satisfaction of one of the foregoing tests, an electing corporation shall not be treated as having a significant business presence in a possession with respect to a product produced in whole or in part by the electing corporation in the possession, for purposes of an election to use the method specified in subparagraph (C)(ii), unless such product is manufactured or produced in the possession by the electing corporation within the meaning of subsection (d)(1)(A) of section 954.

"(ii) SPECIAL RULES.—

"(I) An electing corporation which produces a product or renders a type of service in a possession on the date of the enactment of this clause is not required to meet the significant business presence test in a possession with respect to such product or type of service for its taxable years beginning before January 1, 1986.

"(II) For purposes of this subparagraph, the costs incurred by an electing corporation or any other

member of the affiliated group in connection with contract manufacturing by a person other than a member of the affiliated group, or in connection with a similar arrangement thereto, shall be treated as direct labor costs of the affiliated group and shall not be treated as production costs incurred by the electing corporation in the possession or as direct material costs or as compensation for services performed in the possession, except to the extent as may be otherwise provided in regulations prescribed by the Secretary.

"(iv) REGULATIONS.—The Secretary may prescribe regulations setting forth:

"(I) an appropriate transitional (but not in excess of three taxable years) significant business presence test for commencement in a possession of operations with respect to products or types of service after the date of the enactment of this clause and not described in subparagraph (B)(iii)(I),

"(II) a significant business presence test for other appropriate cases, consistent with the tests specified in subparagraph (B)(ii),

"(III) rules for the definition of a product or type of service, and

"(IV) rules for treating components produced in whole or in part by a related person as materials, and the costs (including direct labor costs) related thereto as a cost of materials, where there is an independent resale price for such components or where otherwise consistent with the intent of the substantial business presence tests.

"(C) METHODS OF COMPUTATION OF TAXABLE INCOME.—If an election of one of the following methods is in effect pursuant to subparagraph (F) with respect to a product or type of service, an electing corporation shall compute its income derived from the active conduct of a trade or business in a possession with respect to such product or type of service in accordance with the method which is elected.

"(i) COST SHARING.—

"(I) PAYMENT OF COST SHARING.—If an election of this method is in effect, the electing corporation must make a payment for its share of the cost (if any) of product area research which is paid or accrued by the affiliated group during that taxable year. Such share shall not be less than the same proportion of the cost of such product area research which the amount of 'possession sales' bears to the amount of 'total sales' of the affiliated group. The cost of product area research paid or accrued solely by the electing corporation in a taxable year (excluding amounts paid directly or indirectly to or on behalf of related persons and excluding amounts paid under any cost sharing agreements with related persons) will reduce (but

not below zero) the amount of the electing corporation's cost sharing payment under this method for that year.

"(a) PRODUCT AREA RESEARCH.—For purposes of this section, the term 'product area research' includes (notwithstanding any provision to the contrary) the research, development and experimental costs, losses, expenses and other related deductions—including amounts paid or accrued for the performance of research or similar activities by another person; qualified research expenses within the meaning of section 44F(b); amounts paid or accrued for the use of, or the right to use, research or any of the items specified in subsection (h)(3)(B)(i); and a proper allowance for amounts incurred for the acquisition of any of the items specified in subsection (h)(3)(B)(i)—which are properly apportioned or allocated to the same product area as that in which the electing corporation conducts its activities, and a ratable part of any such costs, losses, expenses and other deductions which cannot definitely be allocated to a particular product area.

"(b) AFFILIATED GROUP.—For purposes of this subsection, the term 'affiliated group' shall mean the electing corporation and all other organizations, trades or businesses (whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests, within the meaning of section 482.

"(c) POSSESSION SALES.—For purposes of this section, the term 'possession sales' means the aggregate sales or other dispositions for the taxable year to persons who are not members of the affiliated group by members of the affiliated group of products produced, in whole or in part, by the electing corporation in the possession which are in the same product area as is used for determining the amount of product area research, and of services rendered, in whole or in part, in the possession in such product area to persons who are not members of the affiliated group.

"(d) TOTAL SALES.—For purposes of this section, the term 'total sales' means the aggregate sales or other dispositions for the taxable year to persons who are not members of the affiliated group by members of the affiliated group of all products in the same product area as is used for determining the amount of product

area research, and of services rendered in such product area to persons who are not members of the affiliated group.

"(e) Product area.—For purposes of this section, the term 'product area' shall be defined by reference to the three-digit classification of the Standard Industrial Classification code. The Secretary may provide for the aggregation of two or more three-digit classifications where appropriate, and for a classification system other than the Standard Industrial Classification code in appropriate cases.

"(II) Effect of election.—For purposes of determining the amount of its gross income derived from the active conduct of a trade or business in a possession with respect to a product produced by, or type of service rendered by, the electing corporation for a taxable year, if an election of this method is in effect, the electing corporation shall be treated as the owner (for purposes of obtaining a return thereon) of intangible property described in subsection (h)(3)(B)(i) which is related to the units of the product produced, or type of service rendered, by the electing corporation. Such electing corporation shall not be treated as the owner (for purposes of obtaining a return thereon) of any intangible property described in subsection (h)(3)(B)(ii) through (v) (to the extent not described in subsection (h)(3)(B)(i)) or of any other nonmanufacturing intangible. Notwithstanding the preceding sentence, an electing corporation shall be treated as the owner (for purposes of obtaining a return thereon) of (a) intangible property which was developed solely by such corporation in a possession and is owned by such corporation, (b) intangible property described in subsection (h)(3)(B)(i) acquired by such corporation from a person who was not related to such corporation (or to any person related to such corporation) at the time of, or in connection with, such acquisition, and (c) any intangible property described in subsection (h)(3)(B)(ii) through (v) (to the extent not described in subsection (h)(3)(B)(i)) and other nonmanufacturing intangibles which relate to sales of units of products, or services rendered, to unrelated persons for ultimate consumption or use in the possession in which the electing corporation conducts its trade or business.

"(III) Payment provisions.—

"(a) The cost sharing payment determined under subparagraph (C)(i)(I) for any taxable year shall be made to the person or persons specified in subparagraph (C)(i)(IV)(a) not later than the time prescribed by law for filing the electing corporation's return for such taxable

year (including any extensions thereof). If all or part of such payment is not timely made, the amount of the cost sharing payment required to be paid shall be increased by the amount of interest that would have been due under section 6601(a) had the portion of the cost sharing payment that is not timely made been an amount of tax imposed by this title and had the last date prescribed for payment been the due date of the electing corporations's return (determined without regard to any extension thereof). The amount by which a cost sharing payment determined under subparagraph (C)(i)(I) is increased by reason of the preceding sentence shall not be treated as a cost sharing payment or as interest. If failure to make timely payment is due in whole or in part to fraud or willful neglect, the electing corporation shall be deemed to have revoked the election made under subparagraph (A) on the first day of the taxable year for which the cost sharing payment was required.

"(b) For purposes of this title, any tax of a foreign country or possession of the United States which is paid or accrued with respect to the payment or receipt of a cost sharing payment determined under subparagraph (C)(i)(I) or of an amount of increase referred to in subparagraph (C)(i)(III)(a) shall not be treated as income, war profits, or excess profits taxes paid or accrued to a foreign country or possession of the United States, and no deduction shall be allowed under this title with respect to any amounts of such tax so paid or accured.

"(IV) Special rules.—

"(a) The amount of the cost sharing payment determined under subparagraph (C)(i)(I), and any increase in the amount thereof in accordance with subparagraph (C)(i)(III)(a), shall not be treated as income of the recipient, but shall reduce the amount of the deductions (and the amount of reductions in earnings and profits) otherwise allowable to the appropriate domestic member or members (other than an electing corporation) of the affiliated group, or, if there is no such domestic member, to the foreign member or members of such affiliated group as the Secretary may provide under regulations.

"(b) If an election of this method is in effect, the electing corporation shall determine its intercompany pricing under the appropriate section 482 method, provided, however, that an electing corporation shall not be denied use of

the resale price method for purposes of such intercompany pricing merely because the reseller adds more than an insubstantial amount to the value of the product by the use of intangible property.

"(c) The amount of qualified research expenses, within the meaning of section 44F, of any member of the controlled group of corporations (as defined in section 44F(f)) of which the electing corporation is a member shall not be affected by the cost sharing payment required under this method.

"(ii) PROFIT SPLIT.—

"(I) GENERAL RULE.—If an election of this method is in effect, the electing corporation's taxable income derived from the active conduct of a trade or business in a possession with respect to units of a product produced or type of service rendered, in whole or in part, by the electing corporation shall be equal to 50 percent of the combined taxable income of the affiliated group (other than foreign affiliates) derived from covered sales of units of the product produced or type of service rendered, in whole or in part, by the electing corporation in a possession.

"(II) COMPUTATION OF COMBINED TAXABLE INCOME.—Combined taxable income shall be computed separately for each product produced or type of service rendered, in whole or in part, by the electing corporation in a possession. Combined taxable income shall be computed (notwithstanding any provision to the contrary) for each such product or type of service rendered by deducting from the gross income of the affiliated group (other than foreign affiliates) derived from covered sales of such product or type of service all expenses, losses, and other deductions properly apportioned or allocated to gross income from such sales or services, and a ratable part of all expenses, losses, or other deductions which cannot definitely be allocated to some item or class of gross income, which are incurred by the affiliated group (other than foreign affiliates). Notwithstanding any other provision to the contrary, in computing the combined taxable income for each such product or type of service rendered, the research, development, and experimental costs, expenses and related deductions for the taxable year which would otherwise be apportioned or allocated to the gross income of the affiliated group (other than foreign affiliates) derived from covered sales of such product produced or type of service rendered, in whole or in part, by the electing corporation in a possession, shall not be less than the same proportion of the amount of the

share of product area research determined under subparagraph (C)(i)(I) (without regard to the third sentence thereof) in the product area which includes such product or type of service, that such gross income from the product or type of service bears to such gross income from all products produced and types of service rendered, in whole or part, by the electing corporation in a possession.

"(III) DIVISION OF COMBINED TAXABLE INCOME.—50 percent of the combined taxable income computed as provided in subparagraph (C)(ii)(II) shall be allocated to the electing corporation. Combined taxable income, computed without regard to the last sentence of subparagraph (C)(ii)(II), less the amount allocated to the electing corporation under the preceding sentence, shall be allocated to the appropriate domestic member or members (other than any electing corporation) of the affiliated group and shall be treated as income from sources within the United States, or, if there is no such domestic member, to a foreign member or members of such affiliated group as the Secretary may provide under regulations.

"(IV) COVERED SALES.—For purposes of this paragraph, the term 'covered sales' means sales by members of the affilated group (other than foreign affiliates) to persons who are not members of the affiliated group or to foreign affiliates.

"(D) UNRELATED PERSON.—For purposes of this paragraph, the term 'unrelated person' means any person other than a person related within the meaning of paragraph (3)(D) to the electing corporation.

"(E) ELECTING CORPORATION.—For purposes of this subsection, the term 'electing corporation' means a domestic corporation for which an election under this section is in effect.

"(F) TIME AND MANNER OF ELECTION; REVOCATION.—

"(i) IN GENERAL.—An election under subparagraph (A) to use one of the methods under subparagraph (C) shall be made only on or before the due date prescribed by law (including extensions) for filing the tax return of the electing corporation for its first taxable year beginning after December 31, 1982. If an election of one of such methods is made, such election shall be binding on the electing corporation and such method must be used for each taxable year thereafter until such election is revoked by the electing corporation under subparagraph (F)(iii). If any such election is revoked by the electing corporation under subparagraph (F)(iii), such electing corporation may make a subsequent election under subparagraph (A) only with the consent of the Secretary.

"(ii) MANNER OF MAKING ELECTION.—An election under subparagraph (A) to use one of the methods

under subparagraph (C) shall be made by filing a statement to such effect with the return referred to in subparagraph (F)(i) or in such other manner as the Secretary may prescribe by regulations.

"(iii) Revocation.—

"(I) Except as provided in subparagraph (F)(iii)(II), an election may be revoked for any taxable year only with the consent of the Secretary.

"(II) An election shall be deemed revoked for the year in which the electing corporation is deemed to have revoked such election under subparagraph (B)(i) or (C) (i)(III) (a).

"(iv) Aggregation.—

"(I) Where more than one electing corporation in the affiliated group produces any product or renders any services in the same product area, all such electing corporations must elect to compute their taxable income under the same method under subparagraph (C).

"(II) All electing corporations in the same affiliated group that produce any products or render any services in the same product area may elect, subject to such terms and conditions as the Secretary may prescribe by regulations, to compute their taxable income from export sales under a different method from that used for all other sales and services. For this purpose, export sales means all sales by the electing corporation of products to foreign persons for use or consumption outside the United States and its possessions, provided such products are manufactured or produced in the possession within the meaning of subsection (d)(1)(A) of section 954, and further provided (except to the extent otherwise provided by regulations) the income derived by such foreign person on resale of such products (in the same state or in an altered state) is not included in foreign base company income for purposes of section 954(a).

"(III) All members of an affiliated group must consent to an election under this subsection at such time and in such manner as shall be prescribed by the Secretary by regulations.

"(6) Treatment of certain sales made after July 1, 1982.—

"(A) In general.—For purposes of this section, in the case of a disposition of intangible property made by a corporation after July 1, 1982, any gain or loss from such disposition shall be treated as gain or loss from sources within the United States to which paragraph (5) does not apply.

"(B) Exception.—Subparagraph (A) shall not apply to any disposition by a corporation of intangible property if such disposition is to a person who is not a related person to such corporation.

"(C) PARAGRAPH DOES NOT AFFECT ELIGIBILITY.—This paragraph shall not apply for purposes of determining whether the corporation meets the requirements of subsection (a)(2).

"(7) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subsection, including rules for the application of this subsection to income from leasing of products to unrelated persons."

(b) INCOME TAX LIABILITY INCURRED TO THE VIRGIN ISLANDS.—Section 934 (relating to limitation on reduction in income tax liability incurred to the Virgin Islands) is amended—

(1) by striking out "50 percent" in subsection (b)(2) and inserting in lieu thereof "65 percent", and

(2) by adding at the end thereof the following new subsections:

"(e) TAX TREATMENT OF INTANGIBLE PROPERTY INCOME OF CERTAIN DOMESTIC CORPORATIONS.—

"(1) IN GENERAL.—

"(A) INCOME ATTRIBUTABLE TO SHAREHOLDER.—The intangible property income (within the meaning of section 936(h)(3)) for any taxable year of any domestic corporation which is described in subsection (b) and which is an inhabitant of the Virgin Islands (within the meaning of section 28(a) of the Revised Organic Act of the Virgin Islands (48 U.S.C. 1642)), shall be included on a pro rata basis in the gross income of all shareholders of such corporation at the close of the taxable year of such corporation as income from sources within the United States for the taxable year of such shareholder in which or with which the taxable year of such corporation ends.

"(B) EXCLUSION FROM THE INCOME OF THE CORPORATION.—Any intangible property income of a corporation described in subparagraph (A) which is included in the gross income of a shareholder of such corporation by reason of subparagraph (A) shall be excluded from the gross income of such corporation.

"(2) FOREIGN SHAREHOLDERS; SHAREHOLDERS NOT SUBJECT TO TAX; INHABITANTS OF THE VIRGIN ISLANDS.—

"(A) IN GENERAL.—Paragraph (1)(A) shall not apply with respect to any shareholder—

"(i) who is not a United States person,

"(ii) who is not subject to tax under this title on intangible property income which would be allocated to such shareholder (but for this subparagraph), or

"(iii) who is an inhabitant of the Virgin Islands.

"(B) TREATMENT OF NONALLOCATED INTANGIBLE PROPERTY INCOME.—For purposes of this subtitle, intangible property income of a corporation described in paragraph (1)(A) which is not included in the gross income of a shareholder of such corporation by reason of subparagraph (A)—

"(i) shall be treated as income from sources within the United States, and

"(ii) shall not be taken into account for purposes of determining whether the conditions specified in paragraph (1) or (2) of subsection (b) are satisfied.

"(3) Distribution to meet qualification requirements.—

"(A) In general.—If the Secretary determines that a corporation does not satisfy a condition specified in paragraph (1) or (2) of subsection (b) for any taxable year by reason of the exclusion from gross income under paragraph (1)(B), such corporation shall nevertheless be treated as satisfying such condition for such year if it makes a pro rata distribution of property after the close of such taxable year to its shareholders (designated at the time of such distribution as a distribution to meet qualification requirements) with respect to their stock in an amount which is equal to—

"(i) if the condition of subsection (b)(1) is not satisfied, that portion of the gross income for the period described in subsection (b)(1)—

"(I) which was not derived from sources within the Virgin Islands, and

"(II) which exceeds the amount of such income for such period which would enable such corporation to satisfy the condition of subsection (b)(1),

"(ii) if the condition of subsection (b)(2) is not satisfied, that portion of the aggregate gross income for such period—

"(I) which was not derived from the active conduct of a trade or business within the Virgin Islands, and

"(II) which exceeds the amount of such income for such period which would enable such corporation to satisfy the conditions of subsection (b)(2), or

"(iii) if neither of such conditions is satisfied, that portion of the gross income which exceeds the amount of gross income for such period which would enable such corporation to satisfy the conditions of paragraphs (1) and (2) of subsection (b).

"(B) Effectively connected income.—In the case of a shareholder who is a nonresident alien individual, an inhabitant of the Virgin Islands, or a foreign corporation, trust, or estate, any distribution described in subparagraph (A) shall be treated as income which is effectively connected with the conduct of a trade or business conducted through a permanent establishment of such shareholder within the United States.

"(C) Distribution denied in case of fraud or willful neglect.—Subparagraph (A) shall not apply to a corporation if the determination of the Secretary described in subparagraph (A) contains a finding that the failure of such corporation to satisfy the conditions in subsection (b) was due in whole or in part to fraud with intent to evade tax or willful neglect on the part of such corporation.

"(4) CERTAIN PROVISIONS OF SECTION 936 TO APPLY.—

"(A) IN GENERAL.—The rules contained in paragraphs (5), (6), and (7) of section 936(h) shall apply to a domestic corporation described in paragraph (1)(A) of this subsection.

"(B) CERTAIN MODIFICATIONS.—For purposes of subparagraph (A), section 936(h) shall be applied by substituting wherever appropriate—

"(i) 'Virgin Islands' for 'possession', and

"(ii) qualification under paragraphs (1) and (2) of subsection (b) for qualification under section 936(a)(2).

"(f) TRANSITIONAL RULE.—In applying subsection (b)(2) with respect to taxable years beginning after December 31, 1982, and before January 1, 1985, the following percentage shall be substituted for '65 percent':

"For taxable years beginning in calendar year:	The percentage is:
1983	55
1984	60".

(c) DENIAL OF DIVIDEND RECEIVED DEDUCTION IN CASE OF A DISTRIBUTION TO MEET QUALIFICATION REQUIREMENTS.—Section 246 (relating to rules applying to deduction for dividends received) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) CERTAIN DISTRIBUTIONS TO SATISFY REQUIREMENTS.—No deduction shall be allowed under section 243(a) with respect to a dividend received pursuant to a distribution described in section 936(h)(4) or 934(e)(3)."

(d) TRANSFER OF INTANGIBLES BY POSSESSION CORPORATION TREATED AS TRANSFER TO AVOID TAXES.—Section 367 (relating to foreign corporations) is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

"(d) SPECIAL RULE RELATING TO TRANSFER OF INTANGIBLES BY POSSESSION CORPORATIONS.—

"(1) IN GENERAL.—If, after August 14, 1982, any possession corporation transfers, directly or indirectly, any intangible property (within the meaning of section 936(h)(3)(B)) to any foreign corporation, such transfer shall be treated for purposes of subsection (a) as pursuant to a plan having as one of its principal purposes the avoidance of Federal income taxes.

"(2) POSSESSION CORPORATION.—

"(A) IN GENERAL.—The term 'possession corporation' means any corporation—

"(i) to which an election under section 936 applies, or

"(ii) which is described in subsection (b) of section 934 and which is an inhabitant of the Virgin Islands (within the meaning of section 28(a) of the Revised Organic Act of the Virgin Islands).

"(B) FORMER POSSESSION CORPORATION.—A corporation shall be treated as a possession corporation with respect to any transfer if such corporation was a possession corporation (within the meaning of subparagraph (A)) at any time during the 5-year period ending on the date of such transfer.

"(3) Transfer by United States affiliates.—A rule similar to the rule of paragraph (1) shall apply in the case of a direct or indirect transfer by a United States affiliate to a foreign person of intangible property which, after August 14, 1982, was being used (or held for use) by a possession corporation under an arrangement with a United States affiliate. For purposes of the preceding sentence, the term "United States affiliate" means any United States person who is a member of an affiliated group (within the meaning of section 936(h)(5)(C)(i)(I)(b)) which includes the possession corporation.

"(4) Waiver authority.—Subject to such terms and conditions as the Secretary may provide, paragraph (1) or (3) shall not apply to any case where the Secretary is satisfied that the transfer will not result in the reduction of current or future Federal income taxes."

(e) Effective Dates.—

(1) In general.—Except as provided in paragraphs (2) and (3), the amendments made by this section shall apply to taxable years beginning after December 31, 1982.

(2) Certain sales made after july 1, 1982.—Paragraph (6) of section 936(h) of the Internal Revenue Code of 1954, and so much of section 934 to which such paragraph applies by reason of section 934(e)(4) of such Code, shall apply to taxable years ending after July 1, 1982.

(3) Certain transfers of intangible is made after august 14, 1982.—Subsection (d) shall apply to taxable years ending after August 14, 1982.

PART IV—TAX-EXEMPT OBLIGATIONS

SEC. 214. MODIFICATION OF EXEMPTION FOR SMALL ISSUES.

(a) Composite Issues.—Paragraph (6) of section 103(b) (relating to exemption for certain small issues) is amended by adding at the end thereof the following new subparagraphs:

"(K) Limitations on treatment of obligations as part of the same issue.—For purposes of this paragraph, separate lots of obligations which (but for this subparagraph) would be treated as part of the same issue shall be treated as separate issues unless the proceeds of such lots are to be used with respect to 2 or more facilities—

"(i) which are located in more than 1 State, or

"(ii) which have, or will have, as the same principal user the same person or related persons.

"(L) Franchises.—For purposes of subparagraph (K), a person (other than a governmental unit) shall be considered a principal user of a facility if such person (or a group of related persons which includes such person)—

"(i) guarantees, arranges, participates in, or assists with the issuance (or pays any portion of the cost of issuance) of any obligation the proceeds of which are to be used to finance or refinance such facility, and

"(ii) provides any property, or any franchise, trademark, or trade name (within the meaning of section

1253), which is to be used in connection with such facility."

(b) Small Issue Exemption Not Allowed Where Obligations Issued as Part of Issue Exempt From Tax Other Than as a Small Issue.—Paragraph (6) of section 103(b), as amended by subsection (a), is amended by adding at the end thereof the following new subparagraph:

"(M) Paragraph not to apply if obligations issued with certain other tax-exempt obligations.—This paragraph shall not apply to any obligation which is issued as part of an issue (other than an issue to which subparagraph (D) applies) if the interest on any other obligation which is part of such issue is excluded from gross income under any provision of law other than this paragraph."

(c) Termination of Small Issue Exemption After December 31, 1986.—Paragraph (6) of section 103(b), as amended by subsections (a) and (b), is amended by adding at the end thereof the following new subparagraph:

"(N) Paragraph not to apply to obligations issued after december 31, 1986.—This paragraph shall not apply to any obligation issued after December 31, 1986 (including any obligation issued to refund an obligation issued on or before such date)."

(d) Exclusion of Certain Research Expenditures From the Limitation on Certain Industrial Development Bonds.—Subparagraph (F) of section 103(b)(6) (relating to exclusion of certain capital expenditures) is amended—

(1) by striking out "or" at the end of clause (ii),

(2) by adding "or" at the end of clause (iii), and

(3) by adding at the end thereof the following new clause:

"(iv) described in clause (i) or (ii) of section 44F(b)(2)(A) for which a deduction was allowed under section 174(a),".

(e) Restrictions on Financing Certain Facilities.—Paragraph (6) of section 103(b) is amended by adding at the end thereof the following new subparagraph:

"(O) Restrictions on financing certain facilities.—This paragraph shall not apply to an issue if—

"(i) more than 25 percent of the proceeds of the issue are used to provide a facility the primary purpose of which is one of the following: retail food and beverage services, automobile sales or service, or the provision of recreation or entertainment; or

"(ii) any portion of the proceeds of the issue is to be used to provide the following: any private or commercial golf course, country club, massage parlor, tennis club, skating facility (including roller skating, skateboard, and ice skating), racquet sports facility (including any handball or racquetball court), hot tub facility, suntan facility, or racetrack."

(f) Effective Dates.—

(1) Composite issues; small issue exemption.—The amendments made by subsections (a) and (b) shall apply to obligations issued after the date of the enactment of this Act.

(2) TERMINATION.—The amendment made by subsection (c) shall take effect on the date of the enactment of this Act.

(3) RESEARCH EXPENDITURES.—The amendment made by subsection (d) shall apply with respect to expenditures made after the date of the enactment of this Act.

(4) CERTAIN FACILITIES.—The amendment made by subsection (e) shall apply to obligations issued after December 31, 1982.

SEC. 215. PUBLIC APPROVAL AND INFORMATION REPORTING REQUIREMENTS APPLICABLE TO PRIVATE ACTIVITY BONDS.

(a) PUBLIC APPROVAL.—Section 103 (relating to interest on certain governmental obligations) is amended by redesignating subsection (k) as subsection (l) and by inserting after subsection (j) the following new subsection:

"(k) PUBLIC APPROVAL FOR INDUSTRIAL DEVELOPMENT BONDS.—

"(1) IN GENERAL.—Notwithstanding subsection (b), an industrial development bond shall be treated as an obligation not described in subsection (a) unless the requirements of paragraph (2) of this subsection are satisfied.

"(2) PUBLIC APPROVAL REQUIREMENT.—

"(A) IN GENERAL.—An obligation shall satisfy the requirements of this paragraph if such obligation is issued as a part of an issue which has been approved by—

"(i) the governmental unit—

"(I) which issued such obligation, or

"(II) on behalf of which such obligation was issued, and

"(ii) each governmental unit having jurisdiction over the area in which any facility, with respect to which financing is to be provided from the proceeds of such issue, is located (except that if more than 1 governmental unit within a State has jurisdiction over the entire area within such State in which such facility is located, only 1 such unit need approve such issue).

"(B) APPROVAL BY A GOVERNMENTAL UNIT.—For purposes of subparagraph (A), an issue shall be treated as having been approved by any governmental unit if such issue is approved—

"(i) by the applicable elected representative of such governmental unit after a public hearing following reasonable public notice, or

"(ii) by voter referendum of such governmental unit.

"(C) SPECIAL RULES FOR APPROVAL OF FACILITY.—If there has been public approval under subparagraph (A) of the plan of financing a facility, such approval shall constitute approval under subparagraph (A) for any issue—

"(i) which is issued pursuant to such plan within 3 years after the date of the first issue pursuant to the approval, and

"(ii) all or substantially all of the proceeds of which are to be used to finance such facility or to refund previous financing under such plan.

"(D) REFUNDING OBLIGATIONS.—No approval under subparagraph (A) shall be necessary with respect to any obliga-

tion which is issued to refund an obligation approved under subparagraph (A) (or treated as approved under subparagraph (C)) unless the maturity date of such obligation is later than the maturity date of the obligation to be refunded.

"(E) Applicable elected representative.—For purposes of this paragraph—

"(i) In general.—The term 'applicable elected representative' means with respect to any governmental unit—

"(I) an elected legislative body of such unit, or

"(II) the chief elected executive officer, the chief elected State legal officer of the executive branch, or any other elected official of such unit designated for purposes of this paragraph by such chief elected executive officer or by State law.

"(ii) No applicable elected representative.—If (but for this clause) a governmental unit has no applicable elected representative, the applicable elected representative for purposes of clause (i) shall be the applicable elected representative of the governmental unit—

"(I) which is the next higher governmental unit with such a representative, and

"(II) from which the authority of the governmental unit with no such representative is derived."

(b) Information Reporting.—

(1) In general.—Section 103 is amended by redesignating subsection (l) as subsection (m) and by adding at the end thereof the following new subsection:

"(l) Information Reporting Requirements For Certain Bonds.—

"(1) In general.—Notwithstanding subsection (b), any industrial development bond or any other obligation which is issued as part of an issue all or a major portion of the proceeds of which are to be used directly or indirectly—

"(A) to finance loans to individuals for educational expenses, or

"(B) by an organization described in section 501(c)(3) which is exempt from taxation by reason of section 501(a),

shall be treated as an obligation not described in paragraph (1) or (2) of subsection (a) unless such bond satisfies the requirements of paragraph (2).

"(2) Information reporting requirement.—An obligation satisfies the requirement of this paragraph if the issuer submits to the Secretary, not later than the 15th day of the 2nd calendar month after the close of the calendar quarter in which the obligation is issued, a statement concerning the issue of which the obligation is a part which contains—

"(A) the name and address of the issuer,

"(B) the date of issue, the amount of lendable proceeds of the issue, and the stated interest rate, term, and face amount of each obligation which is part of the issue,

"(C) where required, the name of the applicable elected representative who approved the issue, or a description of the voter referendum by which the issue was approved,

"(D) the name, address, and employer identification number of—

"(i) each initial principal user of any facilties provided with the proceeds of the issue,

"(ii) the common parent of any affiliated group of corporations (within the meaning of section 1504(a)) of which such initial principal user is a member, and

"(iii) if the issue is treated as a separate issue under subsection (b)(6)(K), any person treated as a principal user under subsection (b)(6)(L), and

"(E) a description of any property to be financed from the proceeds of the issue.

"(3) EXTENSION OF TIME.—The Secretary may grant an extension of time for the filing of any statement required under paragraph (2) if there is reasonable cause for the failure to file such statement in a timely fashion."

(2) CONFORMING AMENDMENT.—Paragraph (2) of section 103(b) (defining industrial development bond) is amended by striking out "For purposes of this subsection" and inserting in lieu thereof "For purposes of this section".

(c) EFFECTIVE DATES.—

(1) PUBLIC APPROVAL.—The amendment made by subsection (a) shall apply to obligations issued after December 31, 1982, other than obligations issued solely to refund any obligation which—

(A) was issued before July 1, 1982, and

(B) has a maturity which does not exceed 3 years.

(2) INFORMATION REPORTING.—The amendments made by subsection (b) shall apply to obligations issued after December 31, 1982 (including any obligation issued to refund an obligation issued before to such date).

SEC. 216. COST RECOVERY FOR CERTAIN PROPERTY FINANCED WITH TAX-EXEMPT BONDS.

(a) COST RECOVERY METHOD.—Subsection (f) of section 168 (relating to special rules for the accelerated cost recovery system) is amended by adding at the end thereof the following new paragraph:

"(12) LIMITATIONS ON PROPERTY FINANCED WITH TAX-EXEMPT BONDS.—

"(A) IN GENERAL.—Notwithstanding any other provision of this section, to the extent that any property is financed by the proceeds of an industrial development bond (within the meaning of section 103(b)(2)) the interest of which is exempt from taxation under section 103(a), the deduction allowed under subsection (a) (and any deduction allowable in lieu of the deduction allowable under subsection (a)) for any taxable year with respect to such property shall be determined under subparagraph (B).

"(B) RECOVERY METHOD.—

"(i) IN GENERAL.—Except as provided in clause (ii), the amount of the deduction allowed with respect to

property described in subparagraph (A) shall be determined by using the straight-line method (with a half-year convention and without regard to salvage value) and a recovery period determined in accordance with the following table:

"In the case of:	*The recovery period is:*
3-year property	*3 years.*
5-year property	*5 years.*
10-year property	*10 years.*
15-year public utility property	*15 years.*

"(ii) 15-YEAR REAL PROPERTY.—In the case of 15-year real property, the amount of the deduction allowed shall be determined by using the straight-line method (determined on the basis of the number of months in the year in which such property was in service and without regard to salvage value) and a recovery period of 15 years.

"(C) EXCEPTIONS.—Subparagraph (A) shall not apply to any recovery property which is placed in service—

"(i) in connection with projects for residential rental property financed by the proceeds of obligations described in section 103(b)(4)(A),

"(ii) in connection with a sewage or solid waste disposal facility—

"(I) which provides sewage or solid waste disposal services for the residents of part or all of 1 or more governmental units, and

"(II) with respect to which substantially all of the sewage or solid waste processed is collected from the general public,

"(iii) as an air or water pollution control facility which is—

"(I) installed in connection with an existing facility, or

"(II) installed in connection with the conversion of an existing facility which uses oil or natural gas (or any product of oil or natural gas) as a primary fuel to a facility which uses coal as a primary fuel, or

"(iv) in connection with a facility with respect to which an urban development action grant has been made under section 119 of the Housing and Community Development Act of 1974.

"(D) EXISTING FACILITY.—For purposes of this paragraph, the term 'existing facility' means a plant or property in operation before July 1, 1982.

"(E) EXCEPTION WHERE LONGER RECOVERY PERIOD APPLICABLE.—Subparagraph (A) shall not apply to any recovery property if the recovery period which would be applicable to such property by reason of an election under subsection (b)(3) exceeds the recovery period for such property determined under subparagraph (B)."

(b) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall apply with respect to property placed in service after December 31, 1982, to the extent such property is financed by the proceeds of an obligation (including a refunding obligation) issued after June 30, 1982.

(2) EXCEPTIONS.—

(A) CONSTRUCTION OR BINDING AGREEMENT.—The amendments made by this section shall not apply with respect to facilities the original use of which commences with the taxpayer and—

(i) the construction, reconstruction, or rehabilitation of which began before July 1, 1982, or

(ii) with respect to which a binding agreement to incur significant expenditures was entered into before July 1, 1982.

(B) REFUNDING.—

(i) IN GENERAL.—Except as provided in clause (ii), in the case of property placed in service after December 31, 1982 which is financed by the proceeds of an obligation which is issued solely to refund another obligation which was issued before July 1, 1982, the amendments made by this section shall apply only with respect to the basis in such property which has not been recovered before the date such refunding obligation is issued.

(ii) SIGNIFICANT EXPENDITURES.—In the case of facilities the original use of which commences with the taxpayer and with respect to which significant expenditures are made before January 1, 1983, the amendments made by this section shall not apply with respect to such facilities to the extent such facilities are financed by the proceeds of an obligation issued solely to refund another obligation which was issued before July 1, 1982.

In the case of an inducement resolution adopted by an issuing authority before July 1, 1982, for purposes of applying subparagraphs (A)(i) and (B)(ii) with respect to obligations described in such resolution, the term "facilities" means the facilities described in such resolution.

(3) CERTAIN PROJECTS FOR RESIDENTIAL REAL PROPERTY.—For purposes of clause (i) of section 168(f)(12)(C) of the Internal Revenue Code of 1954 (as added by this section), any obligation issued to finance a project described in the table contained in paragraph (1) of section 1104(n) of the Mortgage Subsidy Bond Tax Act of 1980 shall be treated as an obligation described in section 103(b)(4)(A) of the Internal Revenue Code of 1954.

SEC. 217. MISCELLANEOUS.

(a) EXEMPT OBLIGATIONS FOR LOCAL DISTRICT HEATING AND COOLING FACILITIES.—

(1) IN GENERAL.—Paragraph (4) of section 103(b) (relating to certain exempt activities) is amended—

(A) by striking out "or" at the end of subparagraph (H),

(B) by striking out the period at the end of subparagraph (I), and inserting in lieu thereof ", or", and

(C) by inserting after subparagraph (I) the following new subparagraph:

"(J) local district heating or cooling facilities."

(2) LOCAL DISTRICT HEATING OR COOLING FACILITIES DEFINED.—Subsection (b) of section 103 is amended by redesignating paragraph (10) as paragraph (13) and by inserting after paragraph (9) the following new paragraph:

"(10) LOCAL DISTRICT HEATING OR COOLING FACILITY.—For purposes of this section—

"(A) IN GENERAL.—The term 'local district heating or cooling facility' means property used as an integral part of a local district heating or cooling system.

"(B) LOCAL DISTRICT HEATING OR COOLING SYSTEM.—

"(i) IN GENERAL.—The term 'local district heating or cooling system' means any local system consisting of a pipeline or network (which may be connected to a heating or cooling source) providing hot water, chilled water, or steam to 2 or more users for—

"(I) residential, commercial, or industrial heating or cooling, or

"(II) process steam.

"(ii) LOCAL SYSTEM.—For purposes of this subparagraph, a local system includes facilities furnishing heating and cooling to an area consisting of a city and one contiguous county."

(3) CONFORMING AMENDMENT.—Subparagraph (C) of section 103(b)(6) is amended by striking out "paragraph (7)" and inserting in lieu thereof "paragraph (13)".

(b) FACILITIES FOR THE LOCAL FURNISHING OF GAS.—Paragraph (4) of section 103(b) is amended by striking out "electric energy from" in the last sentence and inserting in lieu thereof "electric energy or gas from".

(c) QUALIFIED MASS COMMUTING VEHICLE.—Subparagraph (A) of section 103(b)(9) (defining qualified mass commuting vehicle) is amended—

(1) by inserting "ferry," after "rail car", and

(2) by inserting after "mass commuting services" in clause (ii) the phrase "(or, in the case of a ferry, mass transportation services)".

(d) POLLUTION CONTROL FACILITIES ACQUIRED BY REGIONAL POLLUTION CONTROL AUTHORITY.—Subsection (b) of section 103 is amended by inserting after paragraph (10) (as added by subsection (a)) the following new paragraph:

"(11) POLLUTION CONTROL FACILITIES ACQUIRED BY REGIONAL POLLUTION CONTROL AUTHORITIES.—

"(A) IN GENERAL.—For purposes of subparagraph (F) of paragraph (4), an obligation shall be treated as described in such subparagraph if it is part of an issue substantially all of the proceeds of which are used by a qualified regional pollution control authority to acquire existing air or water pollution control facilities which the authority itself will

operate in order to maintain or improve the control of pollutants.

"(B) Restrictions.—Subparagraph (A) shall apply only if—

"(i) the amount paid, directly or indirectly, for the facilities does not exceed their fair market value,

"(ii) the fees or charges imposed, directly or indirectly, on the seller for any use of the facilities after the sale are not less than the amounts that would be charged if the facilities were financed with obligations the interest on which is not exempt from tax, and

"(iii) no person other than the qualified regional pollution control authority is considered after the sale as the owner of the facilities for purposes of Federal income taxes.

"(C) Qualified regional pollution control authority defined.—For purposes of this paragraph, the term 'qualified regional pollution control authority' means an authority which—

"(i) is a political subdivision created by State law to control air or water pollution,

"(ii) has within its jurisdictional boundaries all or part of at least 2 counties (or equivalent political subdivisions), and

"(iii) operates air or water pollution control facilities."

(e) Effective Date.—The amendments made by this section shall apply to obligations issued after the date of the enactment of this Act.

SEC. 218. TREATMENT OF CERTAIN REFUNDING OBLIGATIONS.

(a) General Rule.—Paragraph (1) of section 103(b) of the Internal Revenue Code of 1954 shall not apply to any qualified refunding obligation issued by a qualified issuer after the date of the enactment of this Act.

(b) Qualified Refunding Obligation.—For purposes of subsection (a), a qualified refunding obligation is any obligation issued as part of an issue if—

(1) substantially all of the proceeds of such issue are used to defease refunded bonds which were issued under a pooled security arrangement pursuant to a bond resolution which was adopted in 1974 and under which at least 20 facilities have been financed before 1978, and

(2) each refunded bond is to be retired within 6 months after the first date on which there is no premium for early retirement of such bond.

(c) Qualified Issuer.—For purposes of subsection (a), a qualified issuer is a political subdivision created by a State in 1932 which is engaged primarily in promoting economic development.

SEC. 219. LIMITATION ON MATURITY OF INDUSTRIAL DEVELOPMENT BONDS.

(a) General Rule.—Subsection (b) of section 103 (relating to industrial development bonds) is amended by adding at the end thereof the following new paragraph:

"(14) *MATURITY MAY NOT EXCEED 120 PERCENT OF ECONOMIC LIFE.—*

"(A) *GENERAL RULE.—Paragraphs (4), (5), (6), and (7) shall not apply to any obligation issued as part of an issue if—*

"(i) *the average maturity of the obligations which are part of such issue, exceeds*

"(ii) *120 percent of the average reasonably expected economic life of the facilities being financed with the proceeds of such issue.*

"(B) *DETERMINATION OF AVERAGES.—For purposes of subparagraph (A)—*

"(i) *the average maturity of any issue shall be determined by taking into account the respective issue prices of the obligations which are issued as part of such issue, and*

"(ii) *the average reasonably expected economic life of the facilities being financed with any issue shall be determined by taking into account the respective cost of such facilities.*

"(C) *SPECIAL RULES.—*

"(i) *DETERMINATION OF ECONOMIC LIFE.—For purposes of this paragraph, the reasonably expected economic life of any facility shall be determined as of the later of—*

"(I) *the date on which the obligations are issued, or*

"(II) *the date on which the facility is placed in service (or expected to be placed in service).*

"(ii) *TREATMENT OF LAND.—*

"(I) *LAND NOT TAKEN INTO ACCOUNT.—Except as provided in subclause (II), land shall not be taken into account under subparagraph (A)(ii).*

"(II) *ISSUES WHERE 25 PERCENT OR MORE OF PROCEEDS USED TO FINANCE LAND.—If 25 percent or more of the proceeds of any issue is used to finance land, such land shall be taken into account under subparagraph (A)(ii) and shall be treated as having an economic life of 50 years."*

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to obligations issued after December 31, 1982.

SEC. 220. MORTGAGE SUBSIDY BONDS.

(a) INCREASE IN AMOUNT OF MORTGAGE INTEREST LIMITATION.—

(1) IN GENERAL.—Subparagraph (A) of section 103A(i)(2) (relating to effective rate of mortgage interest) is amended by striking out "1 percentage point" and inserting in lieu thereof "1.125 percentage points".

(2) CLARIFICATION OF PREPAYMENT ASSUMPTIONS.—Clause (iv) of section 103A(i)(2)(B) (relating to prepayment assumptions) is amended to read as follows:

"(iv) *PREPAYMENT ASSUMPTIONS.—In determining the effective rate of interest—*

"(I) it shall be assumed that the mortgage prepayment rate will be the rate set forth in the most recent mortgage maturity experience table published by the Federal Housing Administration for the State (or, if available, the area within the State) in which the residences are located, and

"(II) prepayments of principal shall be treated as received on the last day of the month in which the issuer reasonably expects to receive such prepayments."

(3) CONFORMING AMENDMENTS.—

(A) The paragraph heading of paragraph (2) of section 103A(i) is amended by striking out "1 PERCENTAGE POINT" and inserting in lieu thereof "1.125 PERCENTAGE POINTS".

(B) Subparagraph (C) of section 103A(i)(4) is amended—

(i) by striking out "1 percentage point" in clause (ii) and inserting in lieu thereof "1.125 percentage points", and

(ii) by striking out "1 PERCENTAGE POINT" in the caption and inserting in lieu thereof "1.125 PERCENTAGE POINTS".

(b) DISPOSITION OF NONMORTGAGE INVESTMENT IN CASE OF LOSS.—Paragraph (3) of section 103A(i) (relating to nonmortgage investment requirements) is amended by adding at the end thereof the following new subparagraph:

"(D) NO DISPOSITION IN CASE OF LOSS.—This paragraph shall not require the sale or disposition of any investment if such sale or disposition would result in a loss which exceeds the amount which would be paid or credited to the mortgagors under paragraph (4)(A) (but for such sale or disposition) at the time of such sale or disposition."

(c) REQUIREMENT THAT MORTGAGORS BE FIRST TIME HOMEBUYERS.—Subsection (e) of section 103A (relating to 3-year requirement) is amended to read as follows:

"(e) 3-YEAR REQUIREMENT.—

"(1) IN GENERAL.—An issue meets the requirements of this subsection only if 90 percent or more of the lendable proceeds of such issue are used to finance the residences of mortgagors who had no present ownership interest in their principal residences at any time during the 3-year period ending on the date their mortgage is executed.

"(2) EXCEPTIONS.—For purposes of paragraph (1), the proceeds of an issue which are used—

"(A) to provide financing with respect to targeted area residences,

"(B) to provide qualified home improvement loans, and

"(C) to provide qualified rehabilitation loans,

shall not be taken into account.

"(3) MORTGAGOR'S INTEREST IN RESIDENCE BEING FINANCED.—For purposes of paragraph (1), a mortgagor's interest in the residence with respect to which the financing is being provided shall not be taken into account."

(d) INCREASE IN MAXIMUM PURCHASE PRICE.—Subsection (f) of section 103A (relating to purchase price requirement) is amended—

(1) by striking out "90 percent" each place it appears and inserting in lieu thereof "110 percent" and

(2) by striking out "110 percent" in paragraph (5) and inserting in lieu thereof "120 percent".

(e) TREATMENT OF COOPERATIVE HOUSING CORPORATIONS.—Subsection (l) of section 103A (relating to other definitions and special rules) is amended by adding at the end thereof the following new paragraph:

"(10) COOPERATIVE HOUSING CORPORATIONS.—

"(A) IN GENERAL.—In the case of any cooperative housing corporation—

"(i) each dwelling unit shall be treated as if it were actually owned by the person entitled to occupy such dwelling unit by reason of his ownership of stock in the corporation, and

"(ii) any indebtedness of the corporation allocable to the dwelling unit shall be treated as if it were indebtedness of the shareholder entitled to occupy the dwelling unit.

"(B) ADJUSTMENT TO TARGETED AREA REQUIREMENT.—In the case of any issue to provide financing to a cooperative housing corporation with respect to cooperative housing not located in a targeted area, to the extent provided in regulations, such issue may be combined with 1 or more other issues for purposes of determining whether the requirements of subsection (h) are met.

"(C) COOPERATIVE HOUSING CORPORATION.—The term 'cooperative housing corporation' has the meaning give to such term by section 216(b)(1)."

(f) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to obligations issued after the date of the enactment of this Act.

(2) FIRST TIME HOMEBUYER REQUIREMENT.—The amendments made by subsection (c) shall also apply to obligations issued after April 24, 1979, and before the date of the enactment of this Act but only to the extent that the proceeds of such obligations are not committed as of the date of the enactment of this Act.

SEC. 221. INDUSTRIAL DEVELOPMENT BONDS FOR CERTAIN RESIDENTIAL RENTAL PROPERTY.

(a) IN GENERAL.—Subparagraph (A) of section 103(b)(4) (relating to certain exempt activities) is amended to read as follows:

"(A) projects for residential rental property if each obligation issued pursuant to the issue is in registered form and if at all times during the qualified project period—

"(i) 15 percent or more in the case of targeted area projects, or

"(ii) 20 percent or more in the case of any other project,

of the units in each project are to be occupied by individuals of low or moderate income,".

(b) DEFINITIONS.—Subsection (b) of section 103 (relating to industrial development bonds) is amended by inserting after paragraph (11) the following new paragraph:

"(12) PROJECTS FOR RESIDENTIAL RENTAL PROPERTY.—For purposes of paragraph (4)(A)—

"(A) TARGETED AREA PROJECT.—The term 'targeted area project' means—

"(i) a project located in a qualified census tract (within the meaning of section 103A(k)(2)), or

"(ii) an area of chronic economic distress (within the meaning of section 103A(k)(3)).

"(B) QUALIFIED PROJECT PERIOD.—The term 'qualified project period' means the period beginning on the first day on which 10 percent of the units in the project are occupied and ending on the later of—

"(i) the date which is 10 years after the date on which 50 percent of the units in the project are occupied,

"(ii) the date which is a qualified number of days after the date on which any of the units in the project are occupied, or

"(iii) the date on which any assistance provided with respect to the project under section 8 of the United States Housing Act of 1937 terminates.

For purposes of clause (ii), the term 'qualified number' means, with respect to an obligation described in paragraph (4)(A), 50 percent of the number of days which comprise the term of the obligation with the longest maturity.

"(C) INDIVIDUALS OF LOW AND MODERATE INCOME.—Individuals of low and moderate income shall be determined by the Secretary in a manner consistent with determinations of lower income families under section 8 of the United States Housing Act of 1937 (or if such program is terminated, under such program as in effect immediately before such termination), except that the percentage of median gross income which qualifies as low or moderate income shall be 80 percent."

(c) CONFORMING AMENDMENTS.—

(1) Paragraph (4) of section 103(b) is amended by striking out the second sentence thereof.

(2) Subsection (k) of section 1104 of the Mortgage Subsidy Bond Tax Act of 1980 is hereby repealed.

(d) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to obligations issued after the date of the enactment of this Act.

(2) EXCEPTION.—The amendments made by this section shall not apply with respect to any obligation to which the amendments made by section 1103 of the Mortgage Subsidy Bond Tax Act of 1980 do not apply by reason of section 1104 of such Act.

PART V—MERGERS AND ACQUISITIONS

Subpart A—Changes in Tax Treatment of Partial Liquidations and of Certain Distributions of Appreciated Property

SEC. 222. PARTIAL LIQUIDATIONS.

(a) SECTION 331 (WHICH PROVIDES CAPITAL GAIN OR LOSS TREATMENT FOR SHAREHOLDERS IN LIQUIDATIONS) LIMITED TO COMPLETE LIQUIDATIONS.—Subsection (a) of section 331 (relating to gain or loss to shareholders in corporate liquidations) is amended to read as follows:

"(a) DISTRIBUTIONS IN COMPLETE LIQUIDATION TREATED AS EXCHANGES.—Amounts received by a shareholder in a distribution in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock."

(b) SECTION 336 (WHICH PROVIDES NONRECOGNITION OF GAIN AND LOSS ON DISTRIBUTIONS BY LIQUIDATING CORPORATION) LIMITED TO COMPLETE LIQUIDATIONS.—Subsection (a) of section 336 (relating to distributions of property in liquidation) is amended by striking out "partial or complete liquidation" and inserting in lieu thereof "complete liquidation".

(c) DISTRIBUTIONS TO NONCORPORATE SHAREHOLDERS WHICH QUALIFY AS PARTIAL LIQUIDATIONS UNDER EXISTING LAW TREATED AS REDEMPTIONS.—

(1) Subsection (b) of section 302 (relating to redemptions treated as exchanges) is amended by redesignating paragraph (4) as paragraph (5) and by inserting after paragraph (3) the following new paragraph:

"(4) REDEMPTION FROM NONCORPORATF SHAREHOLDER IN PARTIAL LIQUIDATION.—Subsection (a) shall apply to a distribution if such distribution is—

"(A) in redemption of stock held by a shareholder who is not a corporation, and

"(B) in partial liquidation of the distributing corporation."

(2) Section 302 is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) PARTIAL LIQUIDATION DEFINED.—

"(1) IN GENERAL.—For purposes of subsection (b)(4), a distribution shall be treated as in partial liuidation of a corporation if—

"(A) the distribution is not essentially equivalent to a dividend (determined at the corporate level rather than at the shareholder level), and

"(B) the distribution is pursuant to a plan and occurs within the taxable year in which the plan is adopted or within the succeeding taxable year.

"(2) TERMINATION OF BUSINESS.—The distributions which meet the requirements of paragraph (1)(A) shall include (but shall not be limited to) a distribution which meets the requirements of subparagraphs (A) and (B) of this paragraph:

"(A) The distribution is attributable to the distributing corporation's ceasing to conduct, or consists of the assets of, a qualified trade or business.

"(B) Immediately after the distribution, the distributing corporation is actively engaged in the conduct of a qualified trade or business.

"(3) QUALIFIED TRADE OR BUSINESS.—For purposes of paragraph (2), the term 'qualified trade or business' means any trade or business which—

"(A) was actively conducted throughout the 5-year period ending on the date of the redemption, and

"(B) was not acquired by the corporation within such period in a transaction in which gain or loss was recognized in whole or in part.

"(4) REDEMPTION MAY BE PRO RATA.—Whether or not a redemption meets the requirements of subparagraphs (A) and (B) of paragraph (2) shall be determined without regard to whether or not the redemption is pro rata with respect to all of the shareholders of the corporation.

"(5) TREATMENT OF CERTAIN PASS-THRU ENTITIES.—For purposes of determining under subsection (b)(4) whether any stock is held by a shareholder who is not a corporation, any stock held by a partnership, estate, or trust shall be treated as if it were actually held proportionately by its partners or beneficiaries."

(3) Subsection (a) of section 302 is amended by striking out "paragraph (1), (2), or (3)" and inserting in lieu thereof "paragraph (1), (2), (3), or (4)".

(4) Paragraph (5) of section 302(b) (as redesignated by paragraph (1)) is amended—

(A) by striking out "paragraph (2) or (3)" and inserting in lieu thereof "paragraph (2), (3), or (4)", and

(B) by striking out "paragraph (1) or (2)" and inserting in lieu thereof "paragraph (1), (2), or (4)".

(d) DEFINITION AND SPECIAL RULE.—Section 346 (defining partial liquidation) is amended to read as follows:

"SEC. 346. DEFINITION AND SPECIAL RULE.

"(a) COMPLETE LIQUIDATION.—For purposes of this subchapter, a distribution shall be treated as in complete liquidation of a corporation if the distribution is one of a series of distributions in redemption of all of the stock of the corporation pursuant to a plan.

"(b) TRANSACTIONS WHICH MIGHT REACH SAME RESULT AS PARTIAL LIQUIDATIONS.—The Secretary shall prescribe such regulations as may be necessary to ensure that the purposes of subsections (a) and (b) of section 222 of the Tax Equity and Fiscal Responsibility Act of 1982 (which repeal the special tax treatment for partial liquidations) may not be circumvented through the use of section 355, 351, 337, or any other provision of law or regulations (including the consolidated return regulations)."

(e) TECHNICAL AND CONFORMING AMENDMENTS.—

(1) The following provisions are each amended by striking out "partial or complete liquidation" and inserting in lieu thereof "complete liquidation":

(A) Paragraph (2) of section 306(b) (relating to exceptions).

(B) Subsection (b) of section 331 (relating to nonapplication of section 301).

(C) Subsection (a) of section 334 (relating to basis of property received in liquidations).

(D) Paragraph (1) of section 336(b) (relating to distributions of LIFO inventory).

(2) Subparagraph (B) of section 306(b)(1) (relating to exception for redemptions) is amended by striking out "section 302(b)(3)" and inserting in lieu thereof "paragraph (3) or (4) of section 302(b)".

(3) Subsection (e) of section 312 (relating to special rule for partial liquidation and certain redemptions) is amended—

(A) by striking out "in partial liquidation (whether before, on, or after June 22, 1954) or"; and

(B) by striking out "PARTIAL LIQUIDATIONS AND" in the heading thereof.

(4) Section 338 (as in effect on the day before the date of the enactment of this Act) is hereby repealed.

(5) Paragraph (2) of section 341(a) (relating to collapsible corporations) is amended to read as follows:

"(2) a distribution—

"(A) in complete liquidation of a collapsible corporation if such distribution is treated under this part as in part or full payment in exchange for stock, or

"(B) in partial liquidation (within the meaning of section 302(e)) of a collapsible corporation if such distribution is treated under section 302(b)(4) as in part or full payment in exchange for the stock, and".

(6) Paragraph (1) of section 543(a) (relating to personal holding company income) is amended—

(A) by striking out "and" at the end of subparagraph (A),

(B) by striking out the period at the end of subparagraph (B) and inserting in lieu thereof ", and", and

(C) by adding at the end thereof the following new subparagraph:

"(C) dividends to which section 302(b)(4) would apply if the corporation were an individual."

(7) Paragraph (1) of section 562(b) (relating to distributions in liquidation) is amended by adding at the end thereof the following new sentence:

"For purposes of subparagraph (A), a liquidation includes a redemption of stock to which section 302 applies."

(8)(A) The heading and table of sections for subpart D of part II of subchapter C of chapter 1 are amended to read as follows:

"Subpart D—Definition and Special Rule

"Sec. 346. Definition and special rule."

(B) The item relating to subpart D in table of subparts for such part II is amended to read as follows:

"Subpart D—Definition and special rule."

(f) EFFECTIVE DATES.—

(1) In general.—The amendments made by this section shall apply to distributions after August 31, 1982.

(2) Exceptions.—

(A) Ruling requests.—The amendments made by this section shall not apply to distributions made by any corporation if—

(i)(I) on July 22, 1982, there was a ruling request by such corporation pending with the Internal Revenue Service as to whether such distributions would qualify as a partial liquidation, or

(II) within the period beginning on July 12, 1981, and ending on July 22, 1982, the Internal Revenue Service granted a ruling to such corporation that the distributions would qualify as a partial liquidation, and

(ii) such distributions are pursuant to a plan of partial liquidation adopted before October 1, 1982 (or, if later, 90 days after the date on which the Internal Revenue Service granted a ruling pursuant to the request described in clause (i)(I)).

(B) Plans adopted before July 23, 1982.—The amendments made by this section shall not apply to distributions made pursuant to a plan of partial liquidation adopted before July 23, 1982.

(C) Control acquired after 1981 and before July 23, 1982.—The amendments made by this section shall not apply to distributions made pursuant to a plan of partial liquidation adopted before October 1, 1982, where control of the corporation making the distributions was acquired after December 31, 1981, and before July 23, 1982.

(D) Tender offer of binding contract outstanding on July 22, 1982.—

(i) In general.—The amendments made by this section shall not apply to distributions made by a corporation if—

(I) such distributions are pursuant to a plan of liquidation adopted before October 1, 1982, and

(II) control of such corporation was acquired after July 22, 1982, pursuant to a tender offer or binding contract outstanding on such date.

(ii) Extension of time for adopting plan where acquisition subject to federal regulatory approval.—If the acquisition described in clause (i)(II) is subject to approval by a Federal regulatory agency, clause (i) shall be applied by substituting for "October 1, 1982" the date which is 90 days after the date on which approval by the Federal regulatory agency of such acquisition becomes final.

"(iii) Special rule where offer subject to approval by foreign regulatory body.—In any case where an offer to acquire stock in a corporation was subject to intervention by a foreign regulatory body and a public announcement of such an offer resulted in the

intervention by such foreign regulatory body before July 23, 1982—

(I) such public announcement shall be treated as a tender offer, and

(II) clause (i) shall be applied by substituting for "October 1, 1982" the date which is 90 days after the date on which such regulatory body approves a public offer to acquire stock in such corporation.

(iv) SPECIAL RULE WHERE ONE-THIRD OF SHARES ACQUIRED DURING MARCH AND APRIL 1982.—If—

(I) one-third or more of the shares of a corporation were acquired by another corporation during March and April 1982, and

(II) during March or April 1982, the acquiring corporation filed with the Federal Trade Commission notification of its intent to acquire control of the acquired corporation,

subclause (I) of clause (i) shall not apply with respect to distributions made by the acquired corporation.

(E) INSURANCE COMPANIES.—The amendments made by this section shall not apply to distributions made by an insurance company pursuant to a plan of partial liquidation adopted before October 1, 1982, where control was acquired by the distributee or its parent after December 31, 1980, and before July 23, 1982, and the conduct of the insurance business by the distributee is conditioned on approval by a State regulatory authority.

For purposes of this paragraph, the term "control" has the meaning given to such term by section 368(c) of the Internal Revenue Code of 1954.

(3) APPROVAL OF PLAN BY BOARD OF DIRECTORS.—For purposes of—

(A) paragraph (2), and

(B) applying section 346(a)(2) of the Internal Revenue Code of 1954 (as in effect on the day before the date of the enactment of this Act) to distributions to which (but for paragraph (2)) the amendments made by this section would apply,

a plan of liquidation shall be treated as adopted when approved by the corporation's board of directors.

(4) COORDINATION WITH AMENDMENTS MADE BY SECTION 299.—For purposes of section 338(e)(2)(C) of the Internal Revenue Code of 1954 (as added by section 229), any property acquired in a distribution to which the amendments made by this section do not apply by reason of paragraph (2) shall be treated as acquired before September 1, 1982.

SEC. 223. DISTRIBUTION OF APPRECIATED PROPERTY IN REDEMPTION OF STOCK.

(a) AMENDMENTS TO CERTAIN EXCEPTIONS TO RECOGNITION OF GAIN.—

(1) IN GENERAL.—Subparagraphs (A), (B), and (C) of section 311(d)(2) (relating to appreciated property used to redeem stock) are amended to read as follows:

"(A) a distribution to a corporate shareholder if the basis of the property distributed is determined under section 301(d)(2);

"(B) a distribution to which section 302(b)(4) applies and which is made with respect to qualified stock;

"(C) a distribution of stock or an obligation of a corporation if the requirements of paragraph (2) of subsection (e) are met with respect to the distribution;".

(2) DEFINITIONS AND SPECIAL RULES.—Section 311 is amended by adding at the end thereof the following new subsection:

"(e) DEFINITIONS AND SPECIAL RULES FOR SUBSECTION (d)(2).—For purposes of subsection (d)(2) and this subsection—

"(1) QUALIFIED STOCK.—

"(A) IN GENERAL.—The term 'qualified stock' means stock held by a person (other than a corporation) who at all times during the lesser of—

"(i) the 5-year period ending on the date of distribution, or

"(ii) the period during which the distributing corporation (or a predecessor corporation) was in existence,

held at least 10 percent in value of the outstanding stock of the distributing corporation (or predecessor corporation).

"(B) DETERMINATION OF STOCK HELD.—Section 318 shall apply in determining ownership of stock under subparagraph (A); except that, in applying section 318(a)(1), the term 'family' includes any individual described in section 267(c)(4) and any spouse of any such individual.

"(2) DISTRIBUTIONS OF STOCK OR OBLIGATIONS OF CONTROLLED CORPORATIONS.—

"(A) REQUIREMENTS.—A distribution of stock or an obligation of a corporation (hereinafter in this paragraph referred to as the 'controlled corporation') meets the requirements of this paragraph if—

"(i) such distribution is made with respect to qualified stock,

"(ii) substantially all of the assets of the controlled corporation consists of the assets of 1 or more qualified businesses,

"(iii) no substantial part of the controlled corporation's nonbusiness assets were acquired from the distributing corporation, in a transaction to which section 351 applied or as a contribution to capital, within the 5-year period ending on the date of the distribution, and

"(iv) more than 50 percent in value of the outstanding stock of the controlled corporation is distributed by the distributing corporation with respect to qualified stock.

"(B) DEFINITIONS.—For purposes of subparagraph (A)—

"(i) QUALIFIED BUSINESS.—The term 'qualified business' means any trade or business which—

"(I) was actively conducted throughout the 5-year period ending on the date of the distribution, and

"(II) was not acquired by any person within such period in a transaction in which gain or loss was recognized in whole or in part.

"(ii) NONBUSINESS ASSET.—The term 'nonbusiness asset' means any asset not used in the active conduct of a trade or business."

(3) CONFORMING AMENDMENT.—Section 311(d)(2) is amended—

(A) by inserting "and " at the end of subparagraph (E),

(B) by striking out the semicolon and "and" at the end of subparagraph (F) and inserting in lieu thereof a period, and

(C) by striking out subparagraph (G).

(b) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section shall apply to distributions after August 31, 1982.

(2) DISTRIBUTIONS PURSUANT TO RULING REQUESTS BEFORE JULY 23, 1982.—In the case of a ruling request under section 311(d)(2)(A) of the Internal Revenue Code of 1954 (as in effect before the amendments made by this section) made before July 23, 1982, the amendments made by this section shall not apply to distributions made—

(A) pursuant to a ruling granted pursuant to such request, and

(B) within 90 days after the date of such ruling.

(3) DISTRIBUTIONS PURSUANT TO FINAL JUDGMENTS OF COURT.—In the case of a final judgment described in section 311(d)(2)(C) of such Code (as in effect before the amendments made by this section) rendered before July 23, 1982, the amendments made by this section shall not apply to distributions made before January 1, 1986, pursuant to such judgment.

(4) CERTAIN DISTRIBUTIONS WITH RESPECT TO STOCK ACQUIRED BEFORE MAY 1982.—The amendments made by this section shall not apply to distributions—

(A) which meet the requirements of section 311(d)(2)(A) of such Code (as in effect on the day before the date of the enactment of this Act),

(B) which are made on or before August 31, 1983, and

(C) which are made with respect to stock acquired after 1980 and before May 1982.

(5) Distributions of timberland with respect to stock of forest products company.—If—

(A) a forest products company distributes timberland to a shareholder in redemption of the common and preferred stock in such corporation held by such shareholder,

(B) section 311(d)(2)(A) of the Internal Revenue Code of 1954 (as in effect before the amendments made by this section) would have applied to such distributions, and

(C) such distributions are made pursuant to 1 of 2 options contained in a contract between such company and such shareholder which is binding on August 31, 1982, and at all times thereafter,

then such distributions of timberland having an aggregate fair market value on August 31, 1982, not in excess of $10,000,000 shall *be treated as distributions to which section 311(d)(2)(A) of such Code (as in effect before the date of the enactment of this Act) applies.*

Subpart B—Certain Stock Purchases Treated as Asset Purchases

SEC. 224. CERTAIN STOCK PURCHASES TREATED AS ASSET PURCHASES.

(a) General Rule.—Subpart B of part II of subchapter C of chapter 1 (relating to effects on corporation) is amended by adding at the end thereof the following new section:

"SEC. 338. CERTAIN STOCK PURCHASES TREATED AS ASSET ACQUISITIONS.

"(a) General Rule.—For purposes of this subtitle, if a purchasing corporation makes an election under this section (or is treated under subsection (e) as having made such an election), then, in the case of any qualified stock purchase, the target corporation—

"(1) shall be treated as having sold all of its assets at the close of the acquisition date in a single transaction to which section 337 applies, and

"(2) shall be treated as a new corporation which purchased all of the assets referred to in paragraph (1) as of the beginning of the day after the acquisition date.

"(b) Price at Which Deemed Sale Made.—

"(1) In General.—For purposes of subsection (a), the assets of the target corporation shall be treated as sold (and purchased) at an amount equal to—

"(A) the grossed-up basis of the purchasing corporation's stock in the target corporation on the acquisition date,

"(B) properly adjusted under regulations prescribed by the Secretary for liabilities of the target corporation and other relevant items.

"(2) Grossed-up basis.—For purposes of paragraph (1), the grossed-up basis shall be an amount equal to the basis of the purchasing corporation's stock in the target corporation on the acquisition date multiplied by a fraction—

"(A) the numerator of which is 100 percent, and

"(B) the denominator of which is the percentage of stock (by value) of the target corporation held by the purchasing corporation on the acquisition date.

"(3) Allocation among assets.—The amount determined under paragraph (1) shall be allocated among the assets of the target corporation under regulations prescribed by the Secretary.

"(c) Special Rules.—

"(1) COORDINATION WITH SECTION 337 WHERE PURCHASING CORPORATION HOLDS LESS THAN 100 PERCENT OF STOCK.—If during the 1-year period beginning on the acquisition date the maximum percentage (by value) of stock in the target corporation held by the purchasing corporation is less than 100 percent, then in applying section 337 for purposes of subsection (a)(1), the nonrecognition of gain or loss shall be limited to an amount determined by applying such maximum percentage to such gain or loss. The preceding sentence shall not apply if the target corporation is liquidated during such 1-year period.

"(2) Certain redemptions where election made.—If, in connection with a qualified stock purchase with respect to which an election is made under this section, the target corpo-

ration makes a distribution in complete redemption of all of the stock of a shareholder which qualifies under section 302(b)(3) (determined without regard to the application of section 302(c)(2)((A)(ii)), section 336 shall apply to such distribution as if it were a distribution in complete liquidation.

"(d) Purchasing Corporation; Target Corporation; Qualified Stock Purchase.—For purposes of this section—

"(1) Purchasing corporation.—The term 'purchasing corporation' means any corporation which makes a qualified stock purchase of stock of another corporation.

"(2) Target corporation.—The term 'target corporation' means any corporation the stock of which is acquired by another corporation in a qualified stock purchase.

"(3) Qualified stock purchase.—The term 'qualified stock purchase' means any transaction or series of transactions in which stock of 1 corporation possessing—

"(A) at least 80 percent of total combined voting power of all classes of stock entitled to vote, and

"(B) at least 80 percent of the total number of shares of all other classes of stock (except nonvoting stock which is limited and preferred as to dividends),

is acquired by another corporation by purchase during the 12-month acquisition period.

"(e) Deemed Election Where Purchasing Corporation Acquires Asset of Target Corporation.—

"(1) In general.—A purchasing corporation shall be treated as having made an election under this section with respect to any target corporation if, at any time during the consistency period, it acquires any asset of the target corporation (or a target affiliate).

"(2) Exceptions.—Paragraph (1) shall not apply with respect to any acquisition by the purchasing corporation if—

"(A) such acquisition is pursuant to a sale by the target corporation (or the target affiliate) in the ordinary course of its trade or business,

"(B) the basis of the property acquired is determined (in whole or in part) by reference to the adjusted basis of such property in the hands of the person from whom acquired,

"(C) such acquisition was before September 1, 1982,

"(D) to the extent provided in regulations, the property acquired is located outside the United States, or

"(E) such acquisition is described in regulations prescribed by the Secretary.

"(3) Anti-avoidance rule.—Whenever necessary to carry out the purpose of this subsection and subsection (f), the Secretary may treat stock acquisitions which are pursuant to a plan and which meet the 80 percent requirements of subparagraphs (A) and (B) of subsection (d)(3) as qualified stock purchases.

"(f) Consistency Required for All Stock Acquisitions From Same Affiliated Group.—If a purchasing corporation makes qualified stock purchases with respect to the target corporation and 1 or more target affiliates during any consistency period, then (except as otherwise provided in subsection (e))—

"(1) any election under this section with respect to the first such purchase shall apply to each other such purchase, and

"(2) no election may be made under this section with respect to the second or subsequent such purchase if such an election was not made with respect to the first such purchase.

"(g) ELECTION.—

"(1) WHEN MADE.—Except as otherwise provided in regulations, an election under this section shall be made not later than 75 days after the acquisition date.

"(2) MANNER.—An election by the purchasing corporation under this section shall be made in such manner as the Secretary shall by regulations prescribe.

"(3) ELECTION IRREVOCABLE.—An election by a purchasing corporation under this section, once made, shall be irrevocable.

"(h) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) 12-MONTH ACQUISITION PERIOD.—The term '12-month acquisition period' means the 12-month period beginning with the date of the first acquisition by purchase of stock included in a qualified stock purchase.

"(2) ACQUISITION DATE.—The term 'acquisition date' means, with respect to any corporation, the first day on which there is a qualified stock purchase with respect to the stock of such corporation.

"(3) PURCHASE.—

"(A) IN GENERAL.—The term 'purchase' means any acquisition of stock, but only if—

"(i) the basis of the stock in the hands of the purchasing corporation is not determined (I) in whole or in part by reference to the adjusted basis of such stock in the hands of the person from whom acquired, or (II) under section 1014(a) (relating to property acquired from a decedent),

"(ii) the stock is not acquired in an exchange to which section 351 applies, and

"(iii) the stock is not acquired from a person the ownership of whose stock would, under section 318(a) (other than paragaraph (4) thereof), be attributed to the person acquiring such stock.

"(B) DEEMED PURCHASE OF STOCK OF SUBSIDIARIES.—If stock in a corporation is acquired by purchase (within the meaning of subparagraph (A)) and, as a result of such acquisition, the corporation making such purchase is treated (by reason of section 318(a)) as owning stock in a 3rd corporation, the corporation making such purchase shall be treated as having purchased such stock in such 3rd corporation. The corporation making such purchase shall be treated as purchasing stock in the 3rd corporation by reason of the preceding sentence on the first day on which the purchasing corporation is considered under section 318(a) as owning such stock.

"(4) CONSISTENCY PERIOD.—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'consistency period' means the period consisting of—

"(i) the 1-year period before the beginning of the 12-month acquisition period for the target corporation,

"(ii) such acquisition period (up to and including the acquisition date), and

"(iii) the 1-year period beginning on the day after the acquisition date.

"(B) EXTENSION WHERE THERE IS PLAN.—The period referred to in subparagraph (A) shall also include any period during which the Secretary determines that there was in effect a plan to make a qualified stock purchase plus 1 or more other qualified stock purchases (or asset acquisitions described in subsection (e)) with respect to the target corporation or any target affiliate.

"(5) AFFILIATED GROUP.—The term 'affiliated group' has the meaning given to such term by section 1504(a) (determined without regard to the exceptions contained in section 1504(b)).

"(6) TARGET AFFILIATE.—

"(A) IN GENERAL.—A corporation shall be treated as a target affiliate of the target corporation if each of such corporations was, at any time during so much of the consistency period as ends on the acquisition date of the target corporation, a member of an affiliated group which had the same common parent.

"(B) CERTAIN FOREIGN CORPORATIONS, ETC.—Except as otherwise provided in regulations (and subject to such conditions as may be provided in regulations)—

"(i) the term 'target affiliate' does not include a foreign corporation, a DISC, a corporation described in section 934(b), or a corporation to which an election under section 936 applies, and

"(ii) stock held by a target affiliate in a foreign corporation or a domestic corporation which is a DISC or described in section 1248(e) shall be excluded from the operation of this section.

"(7) ACQUISITIONS BY PURCHASING CORPORATION INCLUDE ACQUISITIONS BY CORPORATIONS AFFILIATED WITH PURCHASING CORPORATION.—Except as otherwise provided in regulations, an acquisition of stock or assets by any member of an affiliated group which includes a purchasing corporation shall be treated as made by the purchasing corporation.

"(i) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to ensure that the purposes of this section to require consistency of treatment of stock and asset purchases with respect to a target corporation and its target affiliates (whether by treating all of them as stock purchases or as asset purchases) may not be circumvented through the use of any provision of law or regulations (including the consolidated return regulations)."

(b) REPEAL OF SECTION 334(b)(2).—Subsection (b) of section 334 (relating to limitation of subsidiary) is amended to read as follows:

"(b) LIQUIDATION OF SUBSIDIARY.—

"(1) Distribution in complete liquidation.—If property is received by a corporation in a distribution in a complete liquidation to which section 332(a) applies, the basis of the property in the hands of the distributee shall be the same as it would be in the hands of the transferor.

"(2) Transfers to which section 332(c) applies.—If property is received by a corporation in a transfer to which section 332(c) applies, the basis of the property in the hands of the transferee shall be the same as it would be in the hands of the transferor.

"(3) Distributee defined.—For purposes of this subsection, the term 'distributee' means only the corporation which meets the 80-percent stock ownership requirements specified in section 332(b)."

(c) Technical Amendments.—

(1) Subparagraph (E) of section 168(e)(4) (relating to liquidation of subsidiary, etc.) is amended by adding at the end thereof the following new sentence: "A similar rule shall apply in the case of a deemed liquidation under section 338."

(2) Clause (i) of section 168(f)(10)(B) is amended by striking out "(other than a transaction with respect to which the basis is determined under section 334(b)(2))".

(3) Paragraph (4) of section 318(b) is amended to read as follows:

"(4) section 338(h)(3)(B) (relating to purchase of stock from subsidiaries, etc.);".

(4) Paragraph (2) of section 336(b) is amended by striking out "334(b)(1)" each place it appears and inserting in lieu thereof "334(b)".

(5) Paragraph (2) of section 337(c) (relating to liquidations to which section 332 applies) is amended to read as follows:

"(2) Liquidations to which section 332 applies.—In the case of any sale or exchange following the adoption of a plan of complete liquidation, if section 332 applies with respect to such liquidation, this section shall not apply."

(6) Subsection (d) of section 337 is amended by striking out "subsection (c)(2)(A)" each place it appears and inserting in lieu thereof "subsection (c)(2)".

(7) Paragraph (1) of section 381(a) is amended by striking out ", except in a case in which the basis of the assets distributed is determined under section 334(b)(2)".

(8) Subparagraph (B) of section 617(h)(3) is amended by inserting "338," after "334(b),".

(9) The table of sections for subpart B of part II of subchapter C of chapter 1 is amended by striking out the item relating to section 338 and inserting in lieu thereof the following:

"Sec. 338. Certain stock purchases treated as asset acquisitions."

(d) Effective Dates.—

(1) In general.—The amendments made by this section shall apply to any target corporation (within the meaning of section 338 of the Internal Revenue Code of 1954 as added by this section) with respect to which the acquisition date (within the meaning of such section) occurs after August 31, 1982.

(2) CERTAIN ACQUISITIONS BEFORE SPTEMBER 1, 1982.—

(A) an acquisition date under paragraph (1) occurred after August 31, 1980, and before September 1, 1982,

(B) the target corporation (within the meaning of section 338 of such Code) is not liquidated before september 1, 1982, and

(C) the purchasing corporation (within the meaning of section 338 of such Code) makes, not later than November 15, 1982, and election under section 338 of such Code,

then the amendments made by this section shall apply to the acquisition of such target corporation.

(3) CERTAIN ACQUISITIONS OF FINANCIAL INSTITUTIONS.—In any case in which—

(A) there is, on July 22, 1982, a binding contract to acquire control (within the meaning of section 368(c) of such Code) of any financial institution,

(B) the approval of one or more regulatory authorities is required in order to complete such acquisition, and

(C) within 90 days after the date of the final approval of the last such regulatory authority granting final approval, a plan of complete liquidation of such financial institution is adopted,

then the purchasing corporation may elect not to have the amendments made by this section apply to the acquisition pursuant to such contract.

Subpart C—Miscellaneous Provisions

SEC. 225. CLARIFICATION OF SECTION 368(a)(1)(F).

(a) GENERAL RULE.—Subparagraph (F) of section 368(a)(1) (defining reorganization) is amended by inserting "of one corporation" after "place of organization".

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendment made by subsection (a) shall apply with respect to transactions occurring after August 31, 1982.

(2) PLANS ADOPTED ON OR BEFORE AUGUST 31, 1982.—The amendment made by subsection (a) shall not apply with respect to plans of reorganization adopted on or before August 31, 1982, but only if the transaction occurs before January 1, 1983.

SEC. 226. AMENDMENTS RELATING TO BAILOUTS THROUGH USE OF HOLDING COMPANIES.

(a) AMENDMENTS TO SECTION 304.—

(1) COORDINATION OF SECTIONS 304 AND 351.—

(A) Subsection (b) of section 304 (relating to special rules for application of subsection (a)) is amended by adding at the end thereof the following new paragaph:

"(3) COORDINATION WITH SECTION 351.—

"(A) PROPERTY TREATED AS RECEIVED IN REDEMPTION.—Except as otherwise provided in this paragraph, subsection (a) (and not part III) shall apply to any property received in a distribution described in subsection (a).

"(B) CERTAIN ASSUMPTIONS OF LIABILITY, ETC.—

"(i) IN GENERAL.—Subsection (a) shall not apply to any liability—

"(I) assumed by the acquiring corporation, or

"(II) to which the stock is subject,

if such liability was incurred by the transferor to acquire the stock. For purposes of the preceding sentence, the term 'stock' means stock referred to in paragraph (1)(B) or (2)(A) of subsection (a).

"(ii) EXTENSION OF OBLIGATIONS, ETC.—For purposes of clause (i), an extension, renewal, or refinancing of a liability which meets the requirements of clause (i) shall be treated as meeting such requirements.

"(C) DISTRIBUTIONS INCIDENT TO FORMATION OF BANK HOLDING COMPANIES.—If—

"(i) pursuant to a plan, control of a bank is acquired and within 2 years after the date on which such control is acquired, stock constituting control of such bank is transferred to a BHC in connection with its formation,

"(ii) incident to the formation of the BHC there is a distribution of property described in subsection (a), and

"(iii) the shareholders of the BHC who receive distributions of such property do not have control of such BHC,

then, subsection (a) shall not apply to any securities received by a qualified minority shareholder incident to the formation of such BHC.

"(D) DEFINITIONS AND SPECIAL RULE.—For purposes of subparagraph (C) and this subparagraph—

"(i) QUALIFIED MINORITY SHAREHOLDER.—The term 'qualified minority shareholder' means any shareholder who owns less than 10 percent (in value) of the stock of the BHC. For purposes of the preceding sentence, the rules of paragraph (3) of subsection (c) shall apply.

"(ii) BHC.—The term 'BHC' means a bank holding company (within the meaning of section 2(a) of the Bank Holding Company Act of 1956).

"(iii) SPECIAL RULE IN CASE OF BHC'S FORMED BEFORE 1985.—In the case of a BHC which is formed before 1985, clause (i) of subparagraph (C) shall not apply."

(B) Subsection (f) of section 351 (relating to cross references) is amended by adding at the end thereof the following new paragraph:

"(5) For coordination of this section with section 304, see section 304(b)(3)."

(2) APPLICATION OF SECTION 304 WHERE STOCK IS ACQUIRED IN THE TRANSACTION.—

"(A) Subsection (c) of section 304 is amended by redesignating paragraph (2) as paragraph (3) and by inserting after paragraph (1) the following new paragraph:

"(2) STOCK ACQUIRED IN THE TRANSACTION.—For purposes of subsection (a)(1)—

"(A) GENERAL RULE.—Where 1 or more persons in control of the issuing corporation transfer stock of such corporation in exchange for stock of the acquiring corporation, the stock of the acquiring corporation received shall be taken into ac-

count in determining whether such person or persons are in control of the acquiring corporation.

"(B) DEFINITION OF CONTROL GROUP.—Where 2 or more persons in control of the issuing corporation transfer stock of such corporation to the acquiring corporation and, after the transfer, the transferors are in control of the acquiring corporation, the person or persons in control of each corporation shall include each of the persons who so transfer stock."

(B) Paragraph (3) of section 304(c) (as redesignated by paragraph (1)) is amended by striking out "paragraph (1)" and inserting in lieu thereof "this section".

(3) DETERMINATION OF EARNINGS AND PROFITS.—Subparagraph (A) of section 304(b)(2) (relating to amount constituting dividend) is amended to read as follows:

"(A) WHERE SUBSECTION (a)(1) APPLIES.—In the case of any acquisition of stock to which paragraph (1) (and not paragraph (2)) of subsection (A) of this section applies, the determination of the amount which is a dividend shall be made as if the property were distributed by the issuing corporation to the acquiring corporation and immediately thereafter distributed by the acquiring corporation."

(b) APPLICATION OF SECTION 306 TO CERTAIN STOCK ACQUIRED IN SECTION 351 EXCHANGES.—Subsection (c) of section 306 (defining section 306 stock) is amended by adding at the end thereof the following new paragraph:

"(3) CERTAIN STOCK ACQUIRED IN SECTION 351 EXCHANGE.—The term 'section 306 stock' also includes any stock which is not common stock acquired in an exchange to which section 351 applied if receipt of money (in lieu of the stock) would have been treated as a dividend to any extent. In the case of such stock, rules similar to the rules of section 304(b)(2) shall apply for purposes of this section."

(c) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to transfers occurring after August 31, 1982, in taxable years ending after such date.

(2) APPROVAL BY FEDERAL RESERVE BOARD.—The amendments made by this section shall not apply to transfers pursuant to an application to form a BHC filed with the Federal Reserve Board before August 16, 1982, if the BHC was formed not later than the later of—

(A) the 90th day after the date of the last required approval of any regulatory authority to form such BHC, or

(B) January 1, 1983.

For purposes of this paragraph, the term "BHC" means a bank holding company (within the meaning of section 2(a) of the Bank Holding Company Act of 1956).

SEC. 227. APPLICATION OF ATTRIBUTION RULES FOR PURPOSES OF SECTIONS 306 AND 356(a)(2).

(a) APPLICATION FOR PURPOSES OF SECTION 306.—Subsection (c) of section 306 is amended by adding at the end thereof the following new paragraph:

"(4) APPLICATION OF ATTRIBUTION RULES FOR CERTAIN PURPOSES.—For purposes of paragraphs (1)(B)(ii) and (3), section 318(a) shall apply. For purposes of applying the preceding sen-

tence to paragraph (3), sections 318(a)(2)(C) and 318(a)(3)(C) shall be applied without regard to the 50 percent limitation contained therein."

(b) Application for Purposes of Section 356(a)(2).—Paragraph (2) of section 356(a) (relating to treatment as dividend) is amended by inserting "(determined with the application of section 318(a))" after "distribution of a dividend".

(c) Effective Dates.—

(1) Section 306.—The amendment made by subsection (a) shall apply to stock received after August 31, 1982, in taxable years ending after such date.

(2) Section 356.—The amendment made by subsection (b) shall apply to distributions after August 31, 1982, in taxable years ending after such date.

SEC.228 WAIVER OF FAMILY ATTRIBUTION BY ENTITIES.

(a) General Rule.—Paragraph (2) of section 302(c) (relating to constructive ownership of stock) is amended by adding at the end thereof the following new subparagraph:

"(C) Special rule for waivers by entities.—

"(i) In general.—Subparagraph (A) shall not apply to a distribution to any entity unless—

"(I) such entity and each related person meet the requirements of clauses (i), (ii), and (iii) of subparagraph (A), and

"(II) each related person agrees to be jointly and severally liable for any deficiency (including interest and additions to tax) resulting from an acquisition described in clause (ii) of subparagraph (A).

In any case to which the preceding sentence applies, the second sentence of subparagraph (A) and subparagraph (B)(ii) shall be applied by substituting 'distributee or any related person' for 'distributee' each place it appears.

"(ii) Definitions.—For purposes of this subparagraph—

"(I) the term 'entity' means a partnership, estate, trust, or corporation; and

"(II) the term 'related person' means any person to whom ownership of stock in the corporation is (at the time of the distribution) attributable under section 318(a)(1) if such stock is further attributable to the entity under section 318(a)(3)."

(b) Effective Date.—The amendment made by subsection (a) shall apply with respect to distributions after August 31, 1982, in taxable years ending after such date.

PART VI—METHODS OF ACCOUNTING

SEC. 229. MODIFICATION OF REGULATIONS ON THE COMPLETED CONTRACT METHOD OF ACCOUNTING.

(a) In General.—The Secretary of the Treasury shall modify the income tax regulations relating to accounting for long-term contracts to—

(1) clarify the time at which a contract is to be considered completed,

(2) clarify when—

(A) one agreement will be treated as more than one contract, and

(B) two or more agreements will be treated as one contract, and

(3) properly allocate all costs which directly benefit, or are incurred by reason of, the extended period long-term contract activities of the taxpayer.

(b) EXTENDED PERIOD LONG-TERM CONTRACTS DEFINED.—For purposes of this section—

(1) IN GENERAL.—The term "extended period long-term contract" means any long-term contract which the taxpayer estimates (at the time such contract is entered into) will not be completed within the 2-year period beginning on the contract commencement date of such contract.

(2) CERTAIN CONSTRUCTION CONTRACTS.—

(A) IN GENERAL.—The term "extended period long-term contract" does not include any construction contract entered into by a taxpayer—

(i) who estimates (at the time such contract is entered into) that such contract will be completed within the 3-year period beginning on the contract commencement date of such contract, or

(ii) whose average annual gross receipts over the 3 taxable years preceding the taxable year in which such contract is entered into do not exceed $25 million.

(B) DETERMINATION OF TAXPAYER'S GROSS RECEIPTS.—For purposes of subparagraph (A), the gross receipts of—

(i) all trades or businesses (whether or not incorporated) which are under common control with the taxpayer (within the meaning of section 52(b)), and

(ii) all members of any controlled group of corporations of which the taxpayer is a member,

for the 3 taxable years of such persons preceding the taxable year in which the contract described in subparagraph (A) is entered into shall be included in the gross receipts of the taxpayer for the period described in subparagraph (A). The Secretary shall prescribe regulations which provide attribution rules that take into account, in addition to the persons and entities described in the preceding sentence, taxpayers who engage in construction contracts through partnerships, joint ventures, and corporations.

(C) CONTROLLED GROUP OF CORPORATIONS.—The term "controlled group of corporations" has the meaning given to such term by section 1563(a), except that—

(i) "more than 50 percent" shall be substituted for "at least 80 percent" each place it appears in section 1563(a)(1), and

(ii) the determination shall be made without regard to subsections (a)(4) and (e)(3)(C) of section 1563.

(3) CONSTRUCTION CONTRACT.—The term "construction contract" means any contract for the building, construction, reconstruction, or rehabilitation of, or the installation of any integral component to, improvements to real property.

(4) CONTRACT COMMENCEMENT DATE.—The term "contract commencement date" means, with respect to any contract, the first date on which any costs (other than costs such as bidding

expenses or expenses incurred in connection with negotiating the contract) allocable to such contract are incurred.

(b) Effective Dates; Special Rules.—

(1) In general.—The modifications to regulations which are required to be made under paragraphs (1) and (2) of subsection (a) shall apply with respect to taxable years ending after December 31, 1982.

(2) Cost allocation.—

(A) In general.—Any modification to Income Tax Regulation 1.451-3 made under subsection (a)(3) which requires additional costs to be allocated to a contract shall apply only to the applicable percentage of such additional costs incurred in taxable years beginning after December 31, 1982, with respect to contracts entered into after such date.

(B) Applicable percentage.—For purposes of subparagraph (A), the applicable percentage shall be determined in accordance with the following table:

"If the taxable year begins in calendar year:	*The applicable percentage is:*
1983	*33⅓*
1984	*66⅔*
1985 or thereafter	*100.".*

"(3) Special rules.—

"(A) Time of completion.—Any contract of a taxpayer which would (but for this paragraph) be treated as having been completed prior to the first taxable year of such taxpayer ending after December 31, 1982, solely by reason of any modification to regulations made under subsection (a)(1), shall be treated as having been completed on the first day of such taxable year.

"(B) Aggregation and severance.—Any contract of a taxpayer which would (but for this paragraph) be treated as having been completed prior to the first taxable year of such taxpayer ending after December 31, 1982—

"(i) solely by reason of any modification to regulations made under subsection (a)(2), or

"(ii) solely by reason of any modifications to regulations made under both paragraphs (1) and (2) of subsection (a), shall be treated as having been completed in the first day after December 31, 1982, on which any contract which was severed from such contract (by reason of the modifications made by subsection (a)(2)) is completed (determined after the application of any modifications to regulations made under subsection (a)(1)).

SEC. 230. ANNUAL ACCRUAL METHOD OF ACCOUNTING EXTENDED TO CERTAIN PARTNERSHIPS.

(a) In General.—Section 447(g) (relating to certain annual accrual accounting methods) is amended—

(1) by inserting "or qualified partnership" after "corporation" each place it appears in paragraph (1),

(2) by amendment paragraph (3) to read as follows:

"(3) Certain nonrecognition transfers.—For purposes of this subsection, if—

"(A) a corporation acquired substantially all the assets of a qualified farming trade or business from another corporation in a transaction in which no gain or loss was recognized to the transferor or transferee corporation, or

"(B) a qualified partnership acquired substantially all the assets of a qualified farming trade or business from one of its partners in a transaction to which section 721 applies,

the transferee corporation or qualified partnership shall be deemed to have computed its taxable income on an annual accrual method of accounting during the period for which the transferor corporation or partnership computed its taxable income from such trade or business on an annual accrual method.", and

(3) by adding at the end thereof the following new paragraph:

"(4) QUALIFIED PARTNERSHIP DEFINED.—For purposes of this subsection—

"(A) QUALIFIED PARTNERSHIP.—The term 'qualified partnership' means a partnership which is engaged in a qualified farming trade or business and each of the partners of which is a corporation other than—

"(i) an electing small business corporation (within the meaning of section 1371(b)), or

"(ii) a personal holding company (within the meaning of section 542(a)).

"(B) QUALIFIED FARMING TRADE OR BUSINESS.—The term 'qualified farming trade or business' means the trade or business of farming sugar cane.".

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

PART VII—ORIGINAL ISSUE DISCOUNT

SEC. 231. ORIGINAL ISSUE DISCOUNT TAKEN INTO ACCOUNT ON BASIS OF CONSTANT INTEREST RATE.

(a) IN GENERAL.—Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by inserting after section 1232 the following new section:

"SEC. 1232A. ORIGINAL ISSUE DISCOUNT.

"(a) Original Issue Discount on Bonds Issued After July 1, 1982, Included in Income on Basis of Constant Interest Rate.—

"(1) GENERAL RULE.—For purposes of this subtitle, there shall be included in the gross income of the holder of any bond having an original issue discount issued after July 1, 1982 (and which is a capital asset in the hands of the holder) an amount equal to the sum of the daily portions of the original issue discount for each day during the taxable year on which such holder held such bond.

"(2) EXCEPTIONS.—Paragraph (1) shall not apply to—

"(A) NATURAL PERSONS.—Any obligation issued by a natural person.

"(B) TAX-EXEMPT OBLIGATIONS.—Any obligation if—

"(i) the interest on such obligation is not includible in gross income under section 103, or

"(ii) the interest on such obligation is exempt from tax (without regard to the identity of the holder) under any other provision of law.

"(C) Short-term government obligations.—Any short-term Government obligation (within the meaning of section 1232(a)(3)).

"(D) United states savings bonds.—Any United States savings bond.

"(3) Determination of daily portions.—For purposes of paragraph (1), the daily portion of the original issue discount on any bond shall be determined by allocating to each day in any bond period its ratable portion of the increase during such bond period in the adjusted issue price of the bond. For purposes of the preceding sentence, the increase in the adjusted issue price for any bond period shall be an amount equal to the excess (if any) of—

"(A) the product of—

"(i) the adjusted issue price of the bond at the beginning of such bond period, and

"(ii) the yield to maturity (determined on the basis of compounding at the close of each bond period), over

"(B) the sum of the amounts payable as interest on such bond during such bond period.

"(4) Adjusted issue price.—For purposes of this subsection, the adjusted issue price of any bond at the beginning of any bond period is the sum of—

"(A) the issue price of such bond, plus

"(B) the adjustments under this subsection to such issue price for all periods before the first day of such bond period.

"(5) Bond period.—Except as otherwise provided in regulations prescribed by the Secretary, the term 'bond period' means a 1-year period (or the shorter period to maturity) beginning on the day in the calendar year which corresponds to the date of original issue of the bond.

"(6) Reduction in case of certain subsequent holders.—For purposes of this subsection, in the case of any purchase of a bond to which this subsection applies after its original issue, the daily portion shall not include an amount (determined at the time of purchase) equal to the excess (if any) of—

"(A) the cost of such bond incurred by the purchaser, over

"(B) the issue price of such bond, increased by the sum of the daily portions for such bond for all days before the date of purchase (computed without regard to this paragraph),

divided by the number of days beginning on the date of such purchase and ending on the day before the stated maturity date.

"(7) Regulation authority.—The Secretary may prescribe regulations providing that where, by reason of varying rates of interest, put or call options, or other circumstances, the inclusion under paragraph (1) for the taxable year does not accurately reflect the income of the holder, the proper amount of income shall be included for such taxable year (and appropriate adjust-

ments shall be made in the amounts included for subsequent taxable years).

"(b) Ratable Inclusion Retained for Corporate Bonds Issued Before July 2, 1982.—

"(1) GENERAL RULE.—There shall be included in the gross income of the holder of any bond issued by corporation after May 27, 1969, and before July 2, 1982 (and which is a capital asset in the hands of the holder)—

"(A) the ratable monthly portion of original issue discount, multiplied by

"(B) the number of complete months (plus any fractional part of a month determined under paragraph (3)) such holder held such bond during the taxable year.

"(2) DETERMINATION OF RATABLE MONTHLY PORTION.—Except as provided in paragraph (4), the ratable monthly portion of original issue discount shall equal—

"(A) the original issue discount, divided by

"(B) the number of complete months from the date of original issue to the stated maturity date of the bond.

"(3) MONTH DEFINED.—For purposes of this subsection, a complete month commences with the date of original issue and the corresponding day of each succeeding calendar month (or the last day of a calendar month in which there is no corresponding day). In any case where a bond is acquired on any day other than a day determined under the preceding sentence, the ratable monthly portion of original issue discount for the complete month (or partial month) in which such acquisition occurs shall be allocated between the transferor and the transferee in accordance with the number of days in such complete (or partial) month each held the bond.

"(4) REDUCTION IN CASE OF CERTAIN SUBSEQUENT HOLDERS.—For purposes of this subsection, the ratable monthly portion of original issue discount shall not include an amount, determined at the time of any purchase after the original issue of the bond, equal to the excess of—

"(A) the cost of such bond incurred by the holder, over

"(B) the issue price of such bond, increased by the portion of original discount previously includible in the gross income of any holder (computed without regard to this paragraph),

divided by the number of complete months (plus any fractional part of a month) from the date of such purchase to the stated maturity date of such bond.

"(c) DEFINITIONS AND SPECIAL RULES.—

"(1) BOND INCLUDES OTHER EVIDENCES OF INDEBTEDNESS.—For purposes of this section, the term 'bond' means a bond, debenture, note, or certificate or other evidence of indebtedness.

"(2) PURCHASE DEFINED.—For purposes of this section, the term 'purchase' means any acquisition of a bond, but only if the basis of the bond is not determined in whole or in part by reference to the adjusted basis of such bond in the hands of the person from whom acquired, or under section 1014(a) (relating to property acquired from a decedent).

"(3) Original issue discount, etc.—For purposes of this section, the terms 'original issue discount', 'issue price', and 'date of original issue' shall have the respective meanings given to such terms by section 1232(b).

"(4) Exceptions.—This section shall not apply to any holder—

"(A) who has purchased the bond at a premium, or

"(B) which is a life insurance company to which section 818(b) applies.

"(5) Basis adjustments.—The basis of any bond in the hands of the holder thereof shall be increased by the amount included in his gross income pursuant to this section."

(b) Deduction Determined on Basis of Constant Interest Rate.—Section 163 (relating to deduction for interest) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) Original Issue Discount.—

"(1) In general.—In the case of any bond issued after July 1, 1982, by an issuer (other than a natural person), the portion of the original issue discount with respect to such bond which is allowable as a deduction to the issuer for any taxable year shall be equal to the aggregate daily portions of the original issue discount for days during such taxable year.

"(2) Definitions and special rules.—For purposes of this section—

"(A) Bond.—The term 'bond' has the meaning given to such term by section 1232A(c)(1).

"(B) Daily portions.—The daily portion of the original issue discount for any day shall be determined under section 1232A(a) (without regard to paragraphs (2)(B) and (6) thereof and without regard to the second sentence of section 1232(b)(1))."

(c) Conforming Amendments.—

(1) Subparagraph (A) of section 1232(a)(2) is amended—

(A) by striking out "by a corporation after May 27, 1969" and inserting in lieu thereof "by a corporation after May 27, 1969, or by a government or political subdivision thereof after July 1, 1982",

(B) by striking out "as provided in paragraph (3)(B)" and inserting in lieu thereof "without regard to subsection (a)(6) or (b)(4) of section 1232A (or the corresponding provisions of prior law)", and

(C) by striking out the subparagraph heading and inserting in lieu thereof the following:

"(A) CORPORATE BONDS ISSUED AFTER MAY 27, 1969, AND GOVERNMENT BONDS ISSUED AFTER JULY 1, 1982.—".

(2) Subparagraph (B) of section 1232(a)(2) is amended—

(A) by striking out "by a government or political subdivision thereof after December 31, 1954" and inserting in lieu thereof "by a government or political subdivision thereof after December 31, 1954, and on or before July 1, 1982,", and

(B) by striking out "GOVERNMENT BONDS" in the subparagraph heading and inserting in lieu thereof "GOVERNMENT BONDS ISSUED ON OR BEFORE JULY 1, 1982".

(3) Subparagraph (D) of section 1232(a)(2) is amended by striking out "This section" and inserting in lieu thereof "This section and sections 1232A and 1232B".

(4) Subsection (a) of section 1232 is amended by striking out paragraph (3) and by redesignating paragraph (4) as paragraph (3).

(d) CLERICAL AMENDMENT.—The table of sections for such part IV is amended by inserting after the item relating to section 1232 the following:

Sec. 1232A. Original issue discount."

(e) TRANSITIONAL RULE.—For purposes of the amendments made by this section, any evidence of indebtedness issued pursuant to a written commitment which was binding on July 1, 1982, and at all times thereafter shall be treated as issued on July 1, 1982.

SEC. 232. TAX TREATMENT OF STRIPPED BONDS.

(a) IN GENERAL.—Part IV of subchapter P of chapter 1 (relating to special rules for determining capital gains and losses) is amended by inserting after section 1232A the following new section:

"SEC. 1232B. TAX TREATMENT OF STRIPPED BONDS.

"(a) INCLUSION IN INCOME AS IF BOND AND COUPONS WERE ORIGINAL ISSUE DISCOUNT BONDS.—If any person purchases after July 1, 1982, a stripped bond or a stripped coupon, then such bond or coupon while held by such purchaser (or by any other person whose basis is determined by reference to the basis in the hands of such purchaser) shall be treated for purposes of section 1232A(a) as a bond originally issued by a corporation on the purchase date and having an original issue discount equal to the excess (if any) of—

"(1) the stated redemption price at maturity (or, in the case of a coupon, the amount payable on the due date of such coupon), over

"(2) such bond's or coupon's ratable share of the purchase price.

For purposes of paragraph (2), ratable shares shall be determined on the basis of their respective fair market values on the date of purchase.

"(b) TAX TREATMENT OF PERSON STRIPPING BOND.—For purposes of this subtitle, if any person strips 1 or more coupons from a bond and after July 1, 1982, disposes of the bond or such coupon—

"(1) such person shall include in gross income an amount equal to the interest accrued on such bond before the time that such coupon or bond was disposed of (to the extent such interest has not theretofore been included in such person's gross income),

"(2) the basis of the bond and coupons shall be increased by the amount of the accrued interest described in paragraph (1),

"(3) the basis of the bond and coupons immediately before the disposition (as adjusted pursuant to paragraph (2)) shall be allocated among the items retained by such person and the items

disposed of by such person on the basis of their respective fair market values, and

"(4) for purposes of subsection (a), such person shall be treated as having purchased on the date of such disposition each such item which he retains for an amount equal to the basis allocated to such item under paragraph (3).

A rule similar to the rule of paragraph (4) shall apply in the case of any person whose basis in any bond or coupon is determined by reference to the basis of the person described in the preceding sentence.

"(c) RETENTION OF EXISTING LAW FOR STRIPPED BONDS PURCHASED BEFORE JULY 2, 1982.—If a bond issued at any time with interest coupons—

"(1) is purchased after August 16, 1954, and before January 1, 1958, and the purchaser does not receive all the coupons which first become payable more than 12 months after the date of the purchase, or

"(2) is purchased after December 31, 1957, and before July 2, 1982, and the purchaser does not receive all the coupons which first become payable after the date of the purchase,

then the gain on the sale or other disposition of such bond by such purchaser (or by a person whose basis is determined by reference to the basis in the hands of such purchaser) shall be considered as ordinary income to the extent that the fair market value (determined as of the time of the purchase) of the bond with coupons attached exceeds the purchase price. If this subsection and section 1232(a)(2)(A) apply with respect to gain realized on the sale or exchange of any evidence of indebtedness, then section 1232(a)(2)(A) shall apply with respect to that part of the gain to which this subsection does not apply.

"(d) SPECIAL RULES FOR TAX-EXEMPT OBLIGATIONS.—In the case of any obligation the interest on which is not includible in gross income under section 103 or is exempt from tax (without regard to the identity of the holder) under any other provision of law—

"(1) subsections (a) and (b)(1) shall not apply,

"(2) the rules of subsection (b)(4) shall apply for purposes of subsection (c), and

"(3) subsection (c) shall be applied without regard to the requirement that the bond be purchased before July 2, 1982.

"(e) DEFINITIONS AND SPECIAL RULES.--For purposes of this section—

"(1) BOND.—The term 'bond' means a bond, debenture, note, or certificate or other evidence of indebtedness.

"(2) STRIPPED BOND.—The term 'stripped bond' means a bond issued at any time with interest coupons where there is a separation in ownership between the bond and any coupon which has not yet become payable.

"(3) STRIPPED COUPON.—The term 'stripped coupon' means any coupon relating to a stripped bond.

"(4) STATED REDEMPTION PRICE AT MATURITY.—The term 'stated redemption price at maturity' has the meaning given such term by the third sentence of section 1232(b)(1).

"(5) COUPON.—The term 'coupon' includes any right to receive interest on a bond (whether or not evidenced by a coupon). This

paragraph shall apply for purposes of subsection (c) only in the case of purchases after July 1, 1982.

"(f) REGULATION AUTHORITY.—The Secretary may prescribe regulations providing that where, by reason of varying rates of interest, put or call options, extendable maturities, or other circumstances, the tax treatment under this section does not accurately reflect the income of the holder of a stripped coupon or stripped bond, or of the person disposing of such bond or coupon, as the case may be, for any period, such treatment shall be modified to require that the proper amount of income be included for such period."

(b) CONFORMING AMENDMENT.—Section 1232 is amended by striking out subsections (c) and (d).

(c) CLERICAL AMENDMENT.—The table of sections for such part IV is amended by inserting after the item relating to section 1232A the following:

"Sec. 1232B. Tax treatment of stripped bonds."

PART VIII—OTHER BUSINESS PROVISIONS

SEC. 233. TARGETED JOBS TAX CREDIT.

(a) TWO YEAR EXTENSION.—Paragraph (3) of section 51(c) (relating to termination of credit for employment of certain new employees) is amended by striking out "1982" and inserting in lieu thereof "1984".

(b) QUALIFIED SUMMER YOUTH EMPLOYEE.—Subsection (d) of section 51 (defining members of targeted groups) is amended—

(1) by striking out "or" at the end of subparagraph (H),

(2) by striking out the period at the end of subparagraph (I) and inserting in lieu thereof ", or",

(3) by inserting after subparagraph (I) the following new subparagraph:

"(J) a qualified summer youth employee.",

(4) by redesignating paragraphs (12), (13), (14), and (15) as paragraphs (13), (14), (15), and (16), respectively, and

(5) by inserting after paragraph (11) the following new paragraph:

"(12) QUALIFIED SUMMER YOUTH EMPLOYEE.—

"(A) IN GENERAL.—The term 'qualified summer youth employee' means an individual—

"(i) who performs services for the employer between May 1 and September 15,

"(ii) who is certified by the designated local agency as having attained age 16 but not 18 on the hiring date (as defined in paragraph (14)),

"(iii) who has not been an employee of the employer during any period prior to the 90-day period described in subparagraph (B)(iii), and

"(iv) who is certified by the designated local agency as being a member of an economically disadvantaged family (as determined under paragraph (11)).

"(B) SPECIAL RULES FOR DETERMINING AMOUNT OF CREDIT.—For purposes of applying this subpart to wages paid or incurred to any qualified summer youth employee—

"(i) subsection (a)(1) shall be applied by substituting '85 percent' for '50 percent',

"(ii) subsections (a)(2) and (b)(3) shall not apply,

"(iii) subsection(b)(2) shall be applied by substituting 'any 90-day period between May 1 and september 15' for 'the 1-year period beginning with the day the individual begins work for the employer', and

(iv) subsection (b)(4) shall be applied by substituting '$3,000' for '$6,000'.

"(C) SPECIAL RULE FOR CONTINUED EMPLOYMENT FOR SAME EMPLOYER.—In the case of an individual who, with respect to the same employer, is certified as a member of another targeted group after such individual has been a qualified summer youth employee, paragraph (14) shall be applied by substituting 'certified' for 'hired by the employer'."

(c) TERMINATION REPEAL OF INVOLUNTARILY TERMINATED CETA EMPLOYEE AS MEMBER OF TARGETED GROUP.—Paragraph (10) of section 51(d) (relating to involuntarily terminated CETA employee) is amended by adding at the end thereof the following new sentence: "This paragraph shall not apply to any individual who begins work for the employer after December 31, 1982."

(d) VOUCHER OR SCRIP PAYMENTS TO GENERAL RECIPIENTS IN QUALIFIED GENERAL ASSISTANCE PROGRAMS.—Subclause (II) of section 51(d)(6)(B)(i) (defining qualified general assistance programs) is amended by inserting before the comma the following: "or voucher or scrip".

(e) ADDITIONAL AUTHORIZATION OF APPROPRIATIONS; REPORTS.—Paragraph (2) of section 261(f) of the Economic Recovery Tax Act of 1981 is amended—

(1) by inserting after "for fiscal year 1982 the sum of $30,000,000" the following: ", and for fiscal years 1983 and 1984 such sums as may be necessary,"; and

(2) by inserting at the end thereof the following new sentence: "The Secretary of Labor shall each calendar year beginning with calendar year 1983 report to the Committee on Ways and Means of the House of Representatives and to the Committee on Finance of the Senate with respect to the results of the testing conducted under subparagraph (A) during the preceding calendar year."

(f) CERTIFICATIONS.—Effective only with respect to individuals who begin work for the taxpayer after May 11, 1982, subparagraph (A) of section 51(d)(15) (relating to special rules for certifications), as in effect before the amendments made by this Act, is amended by striking out "before the day" and inserting in lieu thereof "on or before the day".

(g) EFFECTIVE DATES.—

(1) SUBSECTION (b).—The amendments made by subsection (b) shall apply to amounts paid or incurred after April 30, 1983, to individuals beginning work for the employer after such date.

(2) SUBSECTION (d).—The amendments made by subsection (d) shall apply to amounts paid or incurred after July 1, 1982, to individuals beginning work for the employer after such date.

SEC. 234. ACCELERATED PAYMENT OF INCOME TAX BY CORPORATIONS.

(a) Increase in Amount of Estimated Tax Required To Be Paid.—

(1) In general.—Paragraph (1) of section 6655(b) (relating to amount of underpayment) is amended by striking out "80" each place it appears and inserting in lieu thereof "90."

(2) Conforming amendment.—Paragraph (3) of section 6655(d) (relating to exception to imposition of additional tax) is amended by striking out "80" and inserting in lieu thereof "90".

(b) Elimination of Election With Respect to Payment of Unpaid Taxes.—

(1) In general.—Section 6152 (relating to installment payments of tax) is amended by striking out subsections (a) and (b) and inserting in lieu thereof the following new subsections:

"(a) Privilege To Elect To Make Four Installment Payments By Decedent's Estate.—A decedent's estate subject to the tax imposed by chapter 1 may elect to pay such tax in four equal installments.

"(b) Dates Prescribed for Payment of Four Installments.—In any case (other than payment of estimated income tax) in which the tax may be paid in four installments, the first installment shall be paid on the date prescribed for the payment of the tax, the second installment shall be paid on or before 3 months, the third installment on or before 6 months, and the fourth installment on or before 9 months, after such date.".

(2) Conforming amendments.—

(A) Paragraph (2) of section 832(e) is amended by striking out ", as if no election to make installment payments under section 6152 is made".

(B) Subsection (b) of section 6081 is amended by striking our "or the first installment thereof required under section 6152".

(C) Section 6164 is amended—

(i) by striking out the last sentence of subsection (c) and inserting in lieu thereof the following new sentence: "If an extension of time under this section relates to only a part of the tax, the time for payment of the remainder shall be the date on which payment would have been required if such remainder had been the tax."; and

(ii) by striking out paragraph (2) of subsection (g) and inserting in lieu thereof the following new paragraph:

"(2) the time for payment of such amount shall be considered to be the date on which payment would have been required if there had been no extension with respect to such amount.".

(c) Amount of Addition to Tax.— Subsection (a) of section 6655 (relating to addition to tax) is amended to read as follows:

"(a) Addition to Tax.—Except as provided in subsections (d) and (e), in the case of any underpayment of tax by a corporation—

"(1) In general.—There shall be added to the tax under chapter 1 for the taxable year an amount determined at the rate

established under section 6621 on the amount of the underpayment for the period of the underpayment.

"(2) Special rule where corporation paid 80 percent or more of tax.—In any case in which there would be no underpayment if subsection (b) were applied by substituting '80 percent' for '90 percent' each place it appears, the addition to tax under paragraph (1) shall be equal to 75 percent of the amount otherwise determined under paragraph (1)."

(d) Additional Exception From Penalty for Underpayments of Estimated Income Tax Where a Corporation Has a Recurring Pattern of Seasonal Income.—

(1) In general.—Section 6655 (relating to failure by corporation to pay estimated income tax) is amended by redesignating subsections (e), (f), (g), and (h) as subsections (f), (g), (h), and (i), respectively, and by inserting after subsection (d) the following new subsection:

"(e) Additional Exception for Recurring Seasonal Income.—

"(1) In general.—Notwithstanding the preceding subsections, the addition to the tax with respect to any underpayment of any installment shall not be imposed if the total amount of all payments of estimated tax made on or before the last date prescribed for the payment of such installment equals or exceeds 90 percent of the amount determined under paragraph (2).

"(2) Determination of amount.—The amount determined under this paragraph for any installment shall be determined in the following manner—

"(A) take the taxable income for all months during the taxable year preceding the filing month,

"(B) divide such amount by the base period percentage for all months during the taxable year preceding the filing month,

"(C) determine the tax on the amount determined under subparagraph (B), and

"(D) multiply the tax computed under subparagraph (C) by the base period percentage for the filing month and all months during the taxable year preceding the filing month.

"(3) Definitions and special rules. —For purposes of this subsection—

"(A) Base period percentage.—The base period percentage for any period of months shall be the average percent which the taxable income for the corresponding months in each of the 3 preceding taxable years bears to the taxable income for the 3 preceding taxable years.

"(B) Filing month.—The term 'filing month' means the month in which the installment is required to be paid.

"(C) Limitation on application of subsection.—This subsection shall only apply if the base period percentage for any 6 consecutive months of the taxable year equals or exceeds 70 percent.

"(D) Reorganizations, etc.—The Secretary may by regulations provide for the determination of the base period percentage in the case of reorganizations, new corporations, and other similar circumstances."

(2) Technical amendment.—Subsection (f) of section 6655 (as redesignated by paragraph (1)) is amended by striking out "(d), and (h)" and inserting in lieu thereof "(d), (e), and (i)".

(e) Effective Date.—The amendments made by this section shall apply to taxable years beginning after December 31, 1982.

Subtitle C—Pensions

PART I—CONTRIBUTION AND LOAN LIMITS

SEC. 235. LOWER CONTRIBUTION AND BENEFIT LIMITS FOR CERTAIN ANNUITIES, ETC.

(a) Limit on Annual Defined Benefit Lowered From $136,425 to $90,000; Limit on Annual Defined Contribution Lowered From $45,475 to $30,000.—

(1) Defined benefit plans.—Subparagraph (A) of section 415(b)(1) (relating to limitation for defined benefit plan) is amended by striking out "$75,000" and inserting in lieu thereof "$90,000".

(2) Defined contribution plans.—Subparagraph (A) of section 415(c)(1) (relating to limitation for defined contribution plan) is amended by striking out "$25,000" and inserting in lieu thereof "$30,000".

(3) Conforming amendments.—

(A) Subparagraph (C) of section 415(b)(2) is amended by striking out "$75,000" each place it appears and inserting in lieu thereof "$90,000".

(B) The last sentence of paragraph (7) of section 415(b) is amended by striking out "by substituting '37,500' for '75,000' " and inserting in lieu thereof "by substituting the greater of $68,212 or one-half the amount otherwise applicable for such year under paragraph (1)(A) for '$90,000' ".

(b) Cost-of-Living Adjustments.—

(1) Adjustment to reflect adjustments made in social security benefit payments rather than primary insurance amounts.—Paragraph (1) of section 415(d) (relating to cost-of-living adjustments) is amended by striking out "primary insurance amounts" and inserting in lieu thereof "benefit amounts".

(2) Freeze on cost-of-living adjustments before January 1, 1986.—

(A) In general.—Subsection (d) of section 415 is amended by adding at the end thereof the following new paragraph:

"(3) Freeze on adjustment to defined contribution and benefit limits.—The Secretary shall not make any adjustment under subparagraph (A) or (B) of paragraph (1) with respect to any year beginning after December 31, 1982, and before January 1, 1986."

(B) Change in base period to reflect change in limits and freeze.—Paragraph (2) of section 415(d) (relating to base periods) is amended by striking out "1974" and inserting in lieu thereof "1984".

(3) CONFORMING AMENDMENTS TO DECREASE IN LIMITS.—Paragraph (1) of section 415(d) is amended—

(A) by striking out "$75,000" in subparagraph (A) and inserting in lieu thereof "$90,000", and

(B) by striking out "$25,000" in subparagraph (B) and inserting in lieu thereof "$30,000".

(c) LOWER LIMITS WHERE INDIVIDUAL IS COVERED BY BOTH DEFINED BENEFIT PLAN AND DEFINED CONTRIBUTION PLAN.—

(1) SUM OF DEFINED BENEFIT PLAN FRACTION AND DEFINED CONTRIBUTION PLAN FRACTION CANNOT EXCEED 1.25 FOR DOLLAR LIMITS AND 1.4 FOR PERCENTAGE LIMITS.—Paragraph (1) of section 415(e) (relating to limitation in case of defined benefit plan and defined contribution plan for same employee) is amended by striking out "1.4" and inserting in lieu thereof "1.0".

(2) DEFINED BENEFIT AND CONTRIBUTION PLAN FRACTIONS.—

(A) DEFINED BENEFIT PLAN FRACTION.—Subparagraph (B) of section 415(e)(2) (defining defined benefit plan fraction) is amended to read as follows:

"(B) the denominator of which is the lesser of—

"(i) the product of 1.25, multiplied by the dollar limitation in effect under subsection (b)(1)(A) for such year, or

"(ii) the product of—

"(I) 1.4, multiplied by

"(II) the amount which may be taken into account under subsection (b)(1)(B) with respect to such individual under the plan for such year."

(B) DEFINED CONTRIBUTION PLAN FRACTION.—Subparagraph (B) of section 415(e)(3) (defining defined contribution plan fraction) is amended to read as follows:

"(B) the denominator of which is the sum of the lesser of the following amounts determined for such year and for each prior year of service with the employer:

"(i) the product of 1.25, multiplied by the dollar limitation in effect under subsection (c)(1)(A) for such year (determined without regard to subsection (c)(6)), or

"(ii) the product of—

"(I) 1.4, multiplied by—

"(II) the amount which may be taken into account under subsection (c)(1)(B) (or subsection (c) (7) or (8), if applicable) with respect to such individual under such plan for such year."

(d) TRANSITION RULES FOR DEFINED CONTRIBUTION FRACTION.—Section 415(e) is amended by adding at the end thereof the following new paragraph:

"(6) SPECIAL TRANSITION RULE FOR DEFINED CONTRIBUTION FRACTION FOR YEARS ENDING AFTER DECEMBER 31, 1982.—

"(A) IN GENERAL.—At the election of the plan administrator, in applying paragraph (3) with respect to any year ending after December 31, 1982, the amount taken into account under paragraph (3)(B) with respect to each participant for all years ending before January 1, 1983, shall be an amount equal to the product of—

"(i) the amount determined under paragraph (3)(B) (as in effect for the year ending in 1982) for the year ending in 1982, multiplied by

"(ii) the transition fraction.

"(B) Transition fraction.—The term 'transition fraction' means a fraction—

"(i) the numerator of which is the lesser of—

"(I) $51,875, or

"(II) 1.4, multiplied by 25 percent of the compensation of the participant for the year ending in 1981, and

"(ii) the denominator of which is the lesser of—

"(I) $41,500, or

"(II) 25 percent of the compensation of the participant for the year ending in 1981."

(e) Actuarial Adjustments.—

(1) Actuarial adjustments for early retirement made by reference to age 62 (instead of 55).—Subparagraph (C) of section 415(b)(2) (relating to adjustments where benefit begins before age 55) is amended by striking out "55" each place it appears and inserting in lieu thereof "62".

(2) $75,000 floor on actuarial adjustment where benefit begins before 62.—Subparagraph (C) of section 415(b)(2) is amended by adding at the end thereof the following new sentence: "The reduction under this subparagraph shall not reduce the limitation of paragraph (1)(A) below—

"(i) if the benefit begins at or after age 55, $75,000, or

"(ii) if the benefit begins before age 55, the amount which is the equivalent of the $75,000 limitation for age 55."

(3) Actuarial adjustments where benefit begins after age 65.—Paragraph (2) of section 415(b) is amended by adding at the end thereof the following new subparagraph:

"(D) Adjustment to $90,000 limitation where benefit begins after age 65.—If the retirement income benefit under the plan begins after age 65, the determination as to whether the $90,000 limitation set forth in paragraph (1)(A) has been satisfied shall be made, in accordance with regulations prescribed by the Secretary, by adjusting such benefit so that it is equivalent to such a benefit beginning at age 65."

(4) Limitations on actuarial adjustments under section 415(b)(2).—Paragraph (2) of section 415(b) is amended by adding at the end thereof the following new subparagraph:

"(E) Limitation on certain assumptions.—

"(i) For purposes of adjusting any benefit under subparagraph (B) or (C), the interest rate assumption shall not be less than the greater of 5 percent or the rate specified in the plan.

"(ii) For purposes of adjusting any benefit under subparagraph (D), the interest rate assumption shall not be greater than the lesser of 5 percent or the rate specified in the plan.

"(iii) For purposes of adjusting any benefit under subparagraph (B), (C), or (D), no adjustments under subsection (d)(1) shall be taken into account before the year for which such adjustment first takes effect."

(f) LIMITATIONS ON DEDUCTIBILITY OF CONTRIBUTIONS.—Section 404 (relating to contributions of an employer to an employee's trust, etc.) is amended by adding at the end thereof the following new subsection:

"(j) SPECIAL RULES RELATING TO APPLICATION WITH SECTION 415.—

"(1) NO DEDUCTION IN EXCESS OF SECTION 415 LIMITATION.—In computing the amount of any deduction allowable under paragraph (1), (2), (3), (4), (7), or (10) of subsection (a) for any year—

"(A) in the case of a defined benefit plan, there shall not be taken into account any benefits for any year in excess of any limitation on such benefits under section 415 for such year, or

"(B) in the case of a defined contribution plan, the amount of any contributions otherwise taken into account shall be reduced by any annual additions in excess of the limitation under section 415 for such year.

"(2) NO ADVANCE FUNDING OF COST-OF-LIVING ADJUSTMENTS.—For purposes of clause (i), (ii) or (iii) of subsection (a)(1)(A), and in computing the full funding limitation, there shall not be taken into account any adjustments under section 415(d)(1) for any year before the year for which such adjustment first takes effect."

(g) EFFECTIVE DATES.—

(1) IN GENERAL.—

(A) NEW PLANS.—In the case of any plan which is not in existence on July 1, 1982, the amendments made by this section shall apply to years ending after July 1, 1982.

(B) EXISTING PLANS.—

(i) In the case of any plan which is in existence on July 1, 1982, the amendments made by this section shall apply to years beginning after December 31, 1982.

(ii) PLAN REQUIREMENTS.—A plan shall not be treated as failing to meet the requirements of section 401(a)(16) of the Internal Revenue Code of 1954 for any year beginning before January 1, 1984, merely because such plan provides for benefit or contribution limits which are in excess of the limitations under section 415 of such Code, as amended by this section. The preceding sentence shall not apply to any plan which provides such limits in excess of the limitation under section 415 of such Code before such amendments.

(2) AMENDMENTS RELATED TO COST-OF-LIVING ADJUSTMENTS.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by subsection (b) shall apply to adjustments for years beginning after December 31, 1982.

(B) ADJUSTMENT PROCEDURES.—The amendment made by subsection (b)(1) and (b)(2)(B) shall apply to adjustments for years beginning after December 31, 1985.

(3) TRANSITION RULE WHERE THE SUM OF DEFINED CONTRIBUTION AND DEFINED BENEFIT PLAN FRACTIONS EXCEEDS 1.0.—In the case of a plan which satisfied the requirements of section 415 of the Internal Revenue Code of 1954 for the last year beginning before January 1, 1983, the Secretary of the Treasury or his delegate shall prescribe regulations under which an amount is subtracted from the numerator of the defined contribution plan fraction (not exceeding such numerator) so that the sum of the defined benefit plan fraction and the defined contribution plan fraction computed under section 415(e)(1) of the Internal Revenue Code of 1954 (as amended by the Tax Equity and Fiscal Responsibility Act of 1982) does not exceed 1.0 for such year.

(4) RIGHT TO HIGHER ACCRUED DEFINED BENEFIT PRESERVED.—

(A) IN GENERAL.—In the case of an individual who is a participant before January 1, 1983, in a defined benefit plan which is in existence on July 1, 1982, and with respect to which the requirements of section 415 of such Code have been met for all years, if such individual's current accrued benefit under such plan exceeds the limitation of subsection (b) of section 415 of the Internal Revenue Code of 1954 (as amended by this section), then (in the case of such plan) for purposes of subsections (b) and (e) of such section, the limitation of such subsection (b) with respect to such individual shall be equal to such current accrued benefit.

(B) CURRENT ACCRUED BENEFIT DEFINED.—

(i) IN GENERAL.— For purposes of this paragraph, the term "current accrued benefit" means the individual's accrued benefit (at the close of the last year beginning before January 1, 1983) when expressed as an annual benefit (within the meaning of section 415(b)(2) of such Code as in effect before the amendments made by this Act).

(ii) SPECIAL RULE.—For purposes of determining the amount of any individual's current accrued benefit—

(I) no change in the terms and conditions of the plan after July 1, 1982, and

(II) no cost-of-living adjustment occurring after July 1, 1982,

shall be taken into account.

(5) SPECIAL RULE FOR COLLECTIVE BARGAINING AGREEMENTS.—In the case of a plan maintained on the date of the enactment of this Act pursuant to 1 or more collective bargaining agreements between employee representatives and 1 or more employers, the amendments made by this section and section 253 (relating to age 70½) shall not apply to years beginning before the earlier of—

(A) the date on which the last of the collective bargaining agreements relating to the plan terminates (determined without regard to any extension thereof agreed to after the date of the enactment of this Act), or

(B) January 1, 1986.

For purposes of subparagraph (A), any plan amendment made pursuant to a collective bargaining agreement relating to the plan which amends the plan solely to conform to any requirement added by this section and section 253 shall not be treated as a termination of such collective bargaining agreement.

SEC. 236. LOANS TREATED AS DISTRIBUTIONS.

(a) GENERAL RULE.—Section 72 (relating to annuities and certain proceeds of endowment and life insurance contracts) is amended by redesignating subsection (p) as subsection (q) and by inserting after subsection (o) the following new subsection:

"(p) LOANS TREATED AS DISTRIBUTIONS.—For purposes of this section—

"(1) TREATMENT AS DISTRIBUTIONS.—

"(A) LOANS.—If during any taxable year a participant or beneficiary receives (directly or indirectly) any amount as a loan from a qualified employer plan, such amount shall be treated as having been received by such individual as a distribution under such plan.

"(B) ASSIGNMENTS OR PLEDGES.—If during any taxable year a participant or beneficiary assigns (or agrees to assign) or pledges (or agrees to pledge) any portion of his interest in a qualified employer plan, such portion shall be treated as having been received by such individual as a loan from such plan.

"(2) EXCEPTION FOR CERTAIN LOANS.—

"(A) GENERAL RULE.—Paragraph (1) shall not apply to any loan to the extent that such loan (when added to the outstanding balance of all other loans from such plan whether made on, before, or after August 13, 1982), does not exceed the lesser of—

"(i) $50,000, or

"(ii) ½ of the present value of the nonforfeitable accrued benefit of the employee under the plan (but not less than $10,000).

"(B) REQUIREMENT THAT LOAN BE REPAYABLE WITHIN 5 YEARS.—

"(i) IN GENERAL.—Subparagraph (A) shall not apply to any loan unless such loan, by its terms, is required to be repaid within 5 years.

"(ii) EXCEPTION FOR HOME LOANS.—Clause (i) shall not apply to any loan used to acquire, construct, reconstruct, or substantially rehabilitate any dwelling unit which within a reasonable time is to be used (determined at the time the loan is made) as a principal residence of the participant or a member of the family (within the meaning of section 267(c)(4)) of the participant.

"(C) RELATED EMPLOYERS AND RELATED PLANS.—For purposes of this paragraph—

"(i) the rules of subsections (b), (c), and (m) of section 414 shall apply, and

"(ii) all plans of an employer (determined after the application of such subsections) shall be treated as 1 plan.

"(3) Qualified employer plan, etc.—For purposes of this subsection, the term 'qualified employer plan' means any plan which was (or was determined to be) a qualified employer plan (as defined in section 219(e)(3) without regard to subparagraph (D) thereof). For purposes of this subsection, such term includes any government plan (as defined in section 219(e)(4)).

"(4) Special rules for loans, etc., from certain contracts.—For purposes of this subsection, any amount received as a loan under a contract purchased under a qualified employer plan (and any assignment or pledge with respect to such a contract) shall be treated as a loan under such employer plan."

(b) Technical Amendments.—

(1) Subsection (m) of section 72 is amended by striking out paragraphs (4) and (8).

(2) Subparagraph (A) of section 72(o)(3) is amended by striking out "subsection (m)(4) and (8)" and inserting in lieu thereof "subsection (p)".

(c) Effective Date.—

(1) In general.—The amendments made by this section shall apply to loans, assignments, and pledges made after August 13, 1982. For purposes of the preceding sentence, the outstanding balance of any loan which is renegotiated, extended, renewed, or revised after such date shall be treated as an amount received as a loan on the date of such renegotiation, extension, renewal, or revision.

(2) Exception for certain loans used to repay outstanding obligations.—

(A) In general.—Any qualified refunding loan shall not be treated as a distribution by reason of the amendments made by this section to the extent such loan is repaid before August 14, 1983.

(B) Qualified refunding loan.—For purposes of subparagraph (A), the term "qualified refunding loan" means any loan made after August 13, 1982, and before August 14, 1983, to the extent such loan is used to make a required principal payment.

(C) Required principal payment.—For purposes of subparagraph (B), the term "required principal payment" means any principal repayment on a loan made under the plan which was outstanding on August 13, 1982, if such repayment is required to be made after August 13, 1982, and before August 14, 1983.

PART II—REPEAL OF SPECIAL LIMITATIONS ON PLANS BENEFITING SELF-EMPLOYED INDIVIDUALS OR OWNER-EMPLOYEES

SEC. 237. REPEAL OF SPECIAL QUALIFICATION REQUIREMENTS.

(a) GENERAL RULE.—Subsection (d) of section 401 (relating to additional requirements for qualifications of trusts and plans benefiting owner-employees) is amended—

(1) by striking out paragraphs (1) through (7), and

(2) by redesignating paragraphs (9), (10), and (11) as paragraphs (1), (2), and (3), respectively.

(b) REPEAL OF LIMITATIONS ON AMOUNT OF COMPENSATION TAKEN INTO ACCOUNT AND ON CERTAIN DEFINED BENEFIT PLANS.—Paragraphs (17) and (18) of section 401(a) are hereby repealed.

(c) REPEAL OF EXCISE TAX ON EXCESS CONTRIBUTIONS FOR SELF-EMPLOYED INDIVIDUALS.—

(1) Section 4972 (relating to tax on excess contributions for self-employed individuals) is hereby repealed.

(2) The table of sections for chapter 43 is amended by striking out the item relating to section 4972.

(d) PENALTY FOR PREMATURE WITHDRAWALS LIMITED TO KEY EMPLOYEES IN TOP-HEAVY PLANS.—

(1) Subparagraph (A) of section 72(m)(5) is amended—

(A) by striking out "an owner-employee" the first place it appears and inserting in lieu thereof "a key employee",

(B) by striking out "while he was an owner-employee" and inserting in lieu thereof "while he was a key employee in a top-heavy plan", and

(C) by striking out "an owner-employee" in clause (ii) and inserting in lieu thereof "a key employee".

(2) Paragraph (5) of section 72(m) is amended by adding at the end thereof the following new subparagraph:

"(C) For purposes of this paragraph, the terms 'key employee' and 'top-heavy plan' have the same meaning as when used in section 416."

"(3) Paragraph (6) of section 72(m) is amdend by striking out "except in applying paragraph (5),".

(e) CONFORMING AMENDMENTS.—

(1) Paragraph (10) of section 401(a) is amended to read as follows:

"(10) OTHER REQUIREMENTS.—

"(A) PLANS BENEFITING OWNER-EMPLOYEES.—In the case of any plan which provides contributions or benefits for employees some or all of whom are owner-employees (as defined in subsection (c)(3)), a trust forming part of such plan shall constitute a qualified trust under this section only if the requirements of subsection (d) are also met."

(2) Paragraph (2) of section 404(a) is amended—

(A) by striking out "(8), (11)" and inserting in lieu thereof "(8), (9), (11)", and

(B) by striking out "section 401(a)(9), (10), (17), and (18), and of section 401(d) (other than paragraph (1))" and in-

serting in lieu thereof "section 401(a)(10) and of section 401(d)".

(3)(A) Paragraph (2) of section 408(a) (defining individual retirement account) is amended by striking out "as defined in section 401(d) (1)" and inserting in lieu thereof "as defined in subsection (n)".

(B) Section 408 is amended by redesignating the subsection relating to cross references as subsection (o) and by inserting immediately before such subsection the following new subsection:

"(n) Bank.—For purposes of subsection (a)(2), the term 'bank' means—

"(1) any bank (as defined in section 581),

"(2) an insured credit union (within the meaning of section 101(6) of the Federal Credit Union Act), and

"(3) a corporation which, under the laws of the State of its incorporation, is subject to supervision and examination by the Commissioner of Banking or other officer of such State in charge of the administration of the banking laws of such State.

SEC. 238. REPEAL OF SPECIAL LIMITATIONS ON DEDUCTION FOR SELF-EMPLOYED INDIVIDUALS AND SUBCHAPTER S CORPORATIONS.

(a) Repeal of Limit of Lower of $15,000 or 15 Percent of Earned Income.—Subsection (e) of section 404 (relating to special limitations for self-employed individuals) is amended to read as follows:

"(e) Contributions Allocable to Life Insurance Protection for Self-Employed Individuals.—In the case of a self-employed individual described in section 401(c)(1), contributions which are allocable (determined under regulations prescribed by the Secretary) to the purchase of life, accident, health, or other insurance shall not be taken into account under this section."

(b) Repeal of Limitations on Defined Benefit Plans.—Subsection (j) of section 401 (relating to defined benefit plans providing benefits for self-employed individuals and shareholder-employees) is hereby repealed.

(c) Repeal of Limitations Applicable to Subchapter S Corporations.—Section 1379 is amended—

(1) by striking out subsections (a) and (b), and

(2) by redesignating subsections (c) and (d) as subsections (a) and (b), respectively.

(d) Technical Amendments.—

(1) Paragraph (1) of section 401(c)(1) (defining employee) is amended to read as follows:

"(1) Self-employed individual treated as employee.—

"(A) In general.—The term 'employee' includes, for any taxable year, an individual who is a self-employed individual for such taxable year.

"(B) Self-employed individual.—The term 'self-employed individual' means, with respect to any taxable year, an individual who has earned income (as defined in paragraph (2)) for such taxable year. To the extent provided in regulations prescribed by the Secretary, such term also includes, for any taxable year—

"(i) an individual who would be a self-employed individual within the meaning of the preceding sentence but for the fact that the trade or business carried on by such individual did not have net profits for the taxable year, and

"(ii) an individual who has been a self-employed individual within the meaning of the preceding sentence for any prior taxable year."

(2) Subparagraph (A) of section 401(c)(2) (defining earned income) is amended by striking out "and" at the end of clause (iii), by striking out the period at end of clause (iv) and inserting in lieu thereof ", and", and by adding at the end thereof the following new clause:

"(v) with regard to the deductions allowed by sections 404 and 405(c) to the taxpayer."

(3) Subsection (j) of section 408 is amended to read as follows:

"(j) INCREASE IN MAXIMUM LIMITATIONS FOR SIMPLIFIED EMPLOYEE PENSIONS.—In the case of any simplified employee pension, subsections (a)(1) and (b)(2) of this section shall be applied by increasing the $2,000 amounts contained therein by the amount of the limitation in effect under section 415(c)(1)(A)."

(4)(A) Paragraph (6) of section 408(k) is hereby repealed.

(B) Paragraph (1) of section 408(k) is amended by striking out "(5), and (6)" and inserting in lieu thereof "and (5)".

(C) Subparagraph (C) of section 408(k)(3) is amended to read as follows:

"(C) CONTRIBUTIONS MUST BEAR UNIFORM RELATIONSHIP TO TOTAL COMPENSATION.—For purposes of subparagraph (A), employer contributions to simplified employee pensions shall be considered discriminatory unless contributions thereto bear a uniform relationship to the total compensation (not in excess of the first $200,000) of each employee maintaining a simplified employee pension."

(5) Paragraph (5) of section 415(c) (relating to application with section 404(e)) is hereby repealed.

SEC. 239. ALLOWANCE OF EXCLUSION OF DEATH BENEFIT FOR SELF-EMPLOYED INDIVIDUALS.

Paragraph (3) of section 101(b) (relating to self-employed individual not considered as employee) is amended to read as follows:

"(3) TREATMENT OF SELF-EMPLOYED INDIVIDUALS.—For purposes of this subsection—

"(A) SELF-EMPLOYED INDIVIDUAL NOT CONSIDERED EMPLOYEE.—Except as provided in subparagraph (B), the term 'employee' does not include a self-employed individual described in section 401(c)(1).

"(B) SPECIAL RULE FOR CERTAIN LUMP SUM DISTRIBUTIONS.—In the case of any lump sum distribution described in the second sentence of paragraph (2)(B), the term 'employee' includes a self-employed individual described in section 401(c)(1)."

SEC. 240. SPECIAL RULES FOR TOP HEAVY PLANS.

(a) GENERAL RULE.—Subpart B of part I of subchapter D of chapter 1 (relating to special rules) is amended by adding at the end thereof the following new section:

"SEC. 416. SPECIAL RULES FOR TOP-HEAVY PLANS.

"(a) GENERAL RULE.—A trust shall not constitute a qualified trust under section 401(a) for any plan year if the plan of which it is a part is a top-heavy plan for such plan year unless such plan meets—

"(1) the vesting requirements of subsection (b),

"(2) the minimum benefit requirements of subsection (c), and

"(3) the limitation on compensation requirement of subsection (d).

"(b) VESTING REQUIREMENTS.—

"(1) IN GENERAL.—A plan satisfies the requirements of this subsection if it satisfies the requirements of either of the following subparagraphs:

"(A) 3-YEAR VESTING.—A plan satisfies the requirements of this subparagraph if an employee who has completed at least 3 years of service with the employer or employers maintaining the plan has a nonforfeitable right to 100 percent of his accrued benefit derived from employer contributions.

"(B) 6-YEAR GRADED VESTING.—A plan satisfies the requirements of this subparagraph if an employee has a nonforfeitable right to a percentage of his accrued benefit derived from employer contributions determined under the following table:

"Years of service	The nonforfeitable percentage is:
2	20
3	40
4	60
5	80
6 or more	100

"(2) CERTAIN RULES MADE APPLICABLE.—Except to the extent inconsistent with the provisions of this subsection, the rules of section 411 shall apply for purposes of this subsection.

"(c) PLAN MUST PROVIDE MINIMUM BENEFITS.—

"(1) DEFINED BENEFIT PLANS.—

"(A) IN GENERAL.—A defined benefit plan meets the requirements of this subsection if the accrued benefit derived from employer contributions of each participant who is a non-key employee, when expressed as an annual retirement benefit, is not less than the applicable percentage of the participant's average compensation for years in the testing period.

"(B) APPLICABLE PERCENTAGE.—For purposes of subparagraph (A), the term 'applicable percentage' means the lesser of—

"(i) 2 percent multiplied by the number of years of service with the employer, or

"(ii) 20 percent.

"(C) YEARS OF SERVICE.—For purposes of this paragraph—

"(i) IN GENERAL.—Except as provided in clause (ii), years of service shall be determined under the rules of paragraphs (4), (5), and (6) of section 411(a).

"(ii) EXCEPTION FOR YEARS DURING WHICH PLAN WAS NOT TOP-HEAVY.—A year of service with the employer shall not be taken into account under this paragraph if—

"(I) the plan was not a top-heavy plan for any plan year ending during such year of service, or

"(II) such year of service was completed in a plan year beginning before January 1, 1984.

"(D) AVERAGE COMPENSATION FOR HIGH 5 YEARS.—For purposes of this paragraph—

"(i) IN GENERAL.—A participant's testing period shall be the period of consecutive years (not exceeding 5) during which the participant had the greatest aggregate compensation from the employer.

"(ii) YEAR MUST BE INCLUDED IN YEAR OF SERVICE.—The years taken into account under clause (i) shall be properly adjusted for years not included in a year of service.

"(iii) CERTAIN YEARS NOT TAKEN INTO ACCOUNT.—Except to the extent provided in the plan, a year shall not be taken into account under clause (i) if—

"(I) such year ends in a plan year beginning before January 1, 1984, or

"(II) such year begins after the close of the last year in which the plan was a top-heavy plan.

"(E) ANNUAL RETIREMENT BENEFIT.—For purposes of this paragraph, the term 'annual retirement benefit' means a benefit payable annually in the form of a single life annuity (with no ancillary benefits) beginning at the normal retirement age under the plan.

"(2) DEFINED CONTRIBUTION PLANS.—

"(A) IN GENERAL.—A defined contribution plan meets the requirements of the subsection if the employer contribution for the year for each participant who is a non-key employee is not less than 3 percent of such participant's compensation (within the meaning of section 415).

"(B) SPECIAL RULE WHERE MAXIMUM CONTRIBUTION LESS THAN 3 PERCENT.—

"(i) IN GENERAL.—The percentage referred to in subparagraph (A) for any year shall not exceed the percentage at which contributions are made (or required to be made) under the plan for the year for the key employee for whom such percentage is the highest for the year.

"(ii) DETERMINATION OF PERCENTAGE.—The determination referred to in clause (i) shall be determined for each key employee by dividing the contributions for such employee by so much of his total compensation for the year as does not exceed $200,000.

"(iii) TREATMENT OF AGGREGATION GROUPS.—

"(I) For purposes of this subparagraph, all defined contribution plans required to be included in an aggregation group under subsection (g)(2)(A)(i) shall be treated as one plan.

"(II) This subparagraph shall not apply to any plan required to be included in an aggregation group if such plan enables a defined benefit plan required to be included in such group to meet the requirements of section 401(a)(4) or 410.

"(C) CERTAIN AMOUNTS NOT TAKEN INTO ACCOUNT.—For purposes of this paragraph, any employer contribution attributable to a salary reduction or similar arrangement shall not be taken into account.

"(d) NOT MORE THAN $200,000 IN ANNUAL COMPENSATION TAKEN INTO ACCOUNT.—

"(1) IN GENERAL.—A plan meets the requirements of this subsection if the annual compensation of each employee taken into account under the plan does not exceed the first $200,000.

"(2) COST-OF-LIVING ADJUSTMENTS.—The Secretary shall annually adjust the $200,000 amount contained in paragraph (1) of this subsection and in clause (ii) of subsection (c)(2)(B) in the same manner as he adjusts the dollar amount contained in section 415(c)(1)(A).

"(e) PLAN MUST MEET REQUIREMENTS WITHOUT TAKING INTO ACCOUNT SOCIAL SECURITY AND SIMILAR CONTRIBUTIONS AND BENEFITS.—A top-heavy plan shall not be treated as meeting the requirement of subsection (b) or (c) unless such plan meets such requirement without taking into account contributions or benefits under chapter 2 (relating to tax on self-employment income), chapter 21 (relating to Federal Insurance Contributions Act), title II of the Social Security Act, or any other Federal or State law.

"(f) COORDINATION WHERE EMPLOYER HAS 2 OR MORE PLANS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section where the employer has 2 or more plans including (but not limited to) regulations to prevent inappropriate omissions or require duplication of minimum benefits or contributions.

"(g) TOP-HEAVY PLAN DEFINED.—For purposes of this section—

"(1) IN GENERAL.—

"(A) PLANS NOT REQUIRED TO BE AGGREGATED.—Except as provided in subparagraph (B), the term 'top-heavy plan' means, with respect to any plan year—

"(i) any defined benefit plan if, as of the determination date, the present value of the cumulative accrued benefits under the plan for key employees exceeds 60 percent of the present value of the cumulative accrued benefits under the plan for all employees, and

"(ii) any defined contribution plan if, as of the determination date, the aggregate of the accounts of key employees under the plan exceeds 60 percent of the aggregate of the accounts of all employees under such plan.

"(B) AGGREGATED PLANS.—Each plan of an employer required to be included in an aggregation group shall be

treated as a top-heavy plan if such group is a top-heavy group.

"(2) AGGREGATION.—For purposes of this subsection—

"(A) AGGREGATION GROUP.—

"(i) REQUIRED AGGREGATION.—The term 'aggregation group' means—

"(I) each plan of the employer in which a key employee is a participant, and

"(II) each other plan of the employer which enables any plan described in subclause (I) to meet the requirements of section 401(a)(4) or 410.

"(ii) PERMISSIVE AGGREGATION.—The employer may treat any plan not required to be included in an aggregation group under clause (i) as being part of such group if such group would continue to meet the requirements of sections 401(a)(4) and 410 with such plan being taken into account.

"(B) TOP-HEAVY GROUP.—The term 'top-heavy group' means any aggregation group if—

"(i) the sum (as of the determination date) of—

"(I) the present value of the cumulative accrued benefits for key employees under all defined benefit plans included in such group, and

"(II) the aggregate of the accounts of key employees under all defined contribution plans included in such group,

"(ii) exceeds 60 percent of a similar sum determined for all employees.

"(3) DISTRIBUTIONS DURING LAST 5 YEARS TAKEN INTO ACCOUNT.—For purposes of determining—

"(A) the present value of the cumulative accrued benefit for any employee, or

"(B) the amount of the account of any employee,

such present value or amount shall be increased by the aggregate distributions made with respect to such employee under the plan during the 5-year period ending on the determination date.

"(4) OTHER SPECIAL RULES.—For purposes of this subsection—

"(A) ROLLOVER CONTRIBUTIONS TO PLAN NOT TAKEN INTO ACCOUNT.—Except to the extent provided in regulations, any rollover contribution (or similar transfer) initiated by the employee and made after December 31, 1983, to a plan shall not be taken into account with respect to the transferee plan for purposes of determining whether such plan is a top-heavy plan (or whether any aggregation group which includes such plan is a top-heavy group).

"(B) BENEFITS NOT TAKEN INTO ACCOUNT IF EMPLOYEE CEASES TO BE KEY EMPLOYEE.—If any individual is a non-key employee with respect to any plan for any plan year, but such individual was a key employee with respect to such plan for any prior plan year, any accrued benefit for such employee (and the account of such employee) shall not be taken into account.

“(C) Determination date.—The term ‘determination date’ means, with respect to any plan year—

“(i) the last day of the preceding plan year, or

“(ii) in the case of the first plan year of any plan, the last day of such plan year.

“(D) Years.—To the extent provided in regulations, this section shall be applied on the basis of any year specified in such regulations in lieu of plan years.

“(h) Adjustments in Section 415 Limits for Top-Heavy Plans.—

“(1) In general.—In the case of any top-heavy plan, paragraphs (2)(B) and (3)(B) of section 415(e) shall be applied by substituting ‘1.0’ for ‘1.25’.

“(2) Exception where benefits for key employees do not exceed 90 percent of total benefits and additional contributions are made for non-key employees.—Paragraph (1) shall not apply with respect to any top-heavy plan if the requirements of subparagraphs (A) and (B) of this paragraph are met with respect to such plan.

“(A) Minimum benefit requirements.—

“(i) In general.—The requirements of this subparagraph are met with respect to any top-heavy plan if such plan (and any plan required to be included in an aggregation group with such plan) meets the requirements of subsection (c) as modified by clause (ii).

“(ii) Modifications.—For purposes of clause (i)—

“(I) paragraph (1)(B) of subsection (c) shall be applied by substituting ‘3 percent’ for ‘2 percent’, and by increasing (but not by more than 10 percentage points) 20 percent by 1 percentage point for each year for which such plan was taken into account under this subsection, and

“(II) paragraph (2)(A) shall be applied by substituting ‘4 percent’ for ‘3 percent’.

“(B) Benefits for key employees cannot exceed 90 percent of total benefits.—A plan meets the requirements of this subparagraph if such plan would not be a top-heavy plan if ‘90 percent’ were substituted for ‘60 percent’ each place it appears in paragraphs (1)(A) and (2)(B) of subsection (g).

“(3) Transition rule.—If, but for this paragraph, paragraph (1) would begin to apply with respect to any top-heavy plan, the application of paragraph (1) shall be suspended with respect to any individual so long as there are no—

“(A) employer contributions, forfeitures, or voluntary nondeductible contributions allocated to such individual, or

“(B) accruals for such individual under the defined benefit plan.

“(4) Coordination with transitional rule under section 415.—In the case of any top heavy plan to which paragraph (1) applies, section 415(e)(6)(B)(i) shall be applied by substituting ‘$41,500’ for ‘$51,875’.

“(i) Definitions.—For purposes of this section—

“(1) Key employee.—

"(A) In general.—The term 'key employee' means any participant in an employer plan who, at any time during the plan year or any of the 4 preceding plan years, is—

"(i) an officer of the employer,

"(ii) 1 of the 10 employees owning (or considered as owning within the meaning of section 318) the largest interests in the employer,

"(iii) a 5-percent owner of the employer, or

"(iv) a 1-percent owner of the employer having an annual compensation from the employer of more than $150,000.

For purposes of clause (i), no more than 50 employees (or, if lesser, the greater of 3 or 10 percent of the employees) shall be treated as officers.

"(B) Percentage owners.—

"(i) 5-percent owner.—For purposes of this paragraph, the term '5-percent owner' means—

"(I) if the employer is a corporation, any person who owns (or is considered as owning within the meaning of section 318) more than 5 percent of the outstanding stock of the corporation or stock possessing more than 5 percent of the total combined voting power of all stock of the corporation, or

"(II) if the employer is not a corporation, any person who owns more than 5 percent of the capital or profits interest in the employer.

"(ii) 1-percent owner.—For purposes of this paragraph, the term '1-percent owner' means any person who would be described in clause (i) if '1 percent' were substituted for '5 percent' each place it appears in clause (i).

"(iii) Constructive ownership rules.—For purposes of this subparagraph and subparagraph (A)(ii)(II)—

"(I) subparagraph (C) of section 318(a)(2) shall be applied by substituting '5 percent' for '50 percent', and

"(II) in the case of any employer which is not a corporation, ownership in such employer shall be determined in accordance with regulations prescribed by the Secretary which shall be based on principles similar to the principles of section 318 (as modified by subclause (I)).

"(C) Aggregation rules do not apply for purposes of determining 5-percent or 1-percent owners.—The rules of subsections (b), (c), and (m) of section 414 shall not apply for purposes of determining ownership in the employer.

"(2) Non-key employee.—The term 'non-key employee' means any employee who is not a key employee.

"(3) Self-employed individuals.—In the case of a self-employed individual described in section 401(c)(1)—

"(A) such individual shall be treated as an employee, and

"(B) such individual's earned income (within the meaning of section 401(c)(2)) shall be treated as compensation.

"(4) Treatment of employees covered by collective bargaining agreements.—The requirements of subsections (b), (c), and (d) shall not apply with respect to any employee included in a unit of employees covered by an agreement which the Secretary of Labor finds to be a collective bargaining agreement between employee representatives and 1 or more employers if there is evidence that retirement benefits were the subject of good faith bargaining between such employee representatives and such employer or employers.

"(5) Treatment of beneficiaries.—The terms 'employee' and 'key employee' include their beneficiaries.

"(6) Treatment of simplified employee pensions.—

"(A) Treatment as defined contribution plans.—A simplified employee pension shall be treated as a defined contribution plan.

"(B) Election to have determinations based on employer contributions.—In the case of a simplified employee pension, at the election of the employer, paragraphs (1)(A)(ii) and (2)(B) of subsection (g) shall be applied by taking into account aggregate employer contributions in lieu of the aggregate of the accounts of employees."

(b) Qualification Requirements.—Paragraph (10) of section 401(a) (relating to other requirements) is amended by adding at the end thereof the following new subparagraph:

"(B) Top-heavy plans.—

"(i) In general.—In the case of any top-heavy plan, a trust forming part of such plan shall constitute a qualified trust under this section only if the requirements of section 416 are met.

"(ii) Plans which may become top-heavy.—Except to the extent provided in regulations, a trust forming part of a plan (whether or not a top-heavy plan) shall constitute a qualified trust under this section only if such plan contains provisions—

"(I) which will take effect if such plan becomes a top-heavy plan, and

"(II) which meet the requirements of section 416."

(c) Technical Amendments.—

(1) Subsections (b) and (c) of section 414 (relating to employees of controlled groups) are each amended by striking out "and 415" and inserting in lieu thereof "415, and 416".

(2) Paragraph (4) of section 414(m) (relating to employees of an affiliated service group) is amended by striking out "and 415" in subparagraph (B), and inserting in lieu there of "415, and 416".

(d) Clerical Amendment.—The table of sections for subpart B of part I of subchapter D of chapter 1 is amended by adding at the end there of the following new item:

"Sec. 416. Special rules for top-heavy plans."

SEC. 241. EFFECTIVE DATES.

(a) GENERAL RULE.—Except as provided in subsection (b), the amendments made by this part shall apply to years beginning after December 31, 1983.

(b) ALLOWANCE OF EXCLUSION OF DEATH BENEFIT FOR SELF-EMPLOYED INDIVIDUALS.—The amendment made by section 239 shall apply with respect to decedents dying after December 31, 1983.

PART III—OTHER REQUIREMENTS

SEC. 242. REQUIRED DISTRIBUTIONS FOR QUALIFIED PLANS.

(a) GENERAL RULE.—Paragraph (9) of section 401(a) (relating to requirements for qualification) is amended to read as follows:

"(9) REQUIRED DISTRIBUTIONS.—

"(A) BEFORE DEATH.—A trust forming part of a plan shall not constitute a qualified trust under this section unless the plan provides that the entire interest of each employee—

"(i) either will be distributed to him not later than his taxable year in which he attains age 70½ or, in the case of an employee other than a key employee who is a participant in a top-heavy plan, in which he retires, whichever is the later, or

"(ii) will be distributed, commencing not later than such taxable year—

"(I) in accordance with regulations prescribed by the Secretary, over the life of such employee or over the lives of such employee and his spouse, or

"(II) in accordance with such regulations, over a period not extending beyond the life expectancy of such employee or the life expectancy of such employee and his spouse.

"(B) AFTER DEATH.—A trust forming part of a plan shall not constitute a qualified trust under this section unless the plan provides that if—

"(i) an employee dies before his entire interest has been distributed to him, or

"(ii) distribution has been commenced in accordance with subparagraph (A)(ii) to his surviving spouse and such surviving spouse dies before his entire interest has been distributed to such surviving spouse,

his entire interest (or the remaining part of such interest if distribution thereof has commenced) will be distributed within 5 years after his death (or the death of his surviving spouse). The preceding sentence shall not apply if the distribution of the interest of the employee has commenced and such distribution is for a term certain over a period permitted under subparagraph (A)(ii)(II)."

(b) EFFECTIVE DATE.—

(1) IN GENERAL.—The amendment made by subsection (a) shall apply to plan years beginning after December 31, 1983.

(2) TRANSITION RULE.—A trust forming part of a plan shall not be disqualified under paragraph (9) of section 401(a) of the

Internal Revenue Code of 1954, as amended by subsection (a), by reason of distributions under a designation (before January 1, 1984) by any employee of a method of distribution—

(A) which does not meet the requirements of such paragraph (9), but

(B) which would not have disqualified such trust under paragraph (9) of section 401(a) of such Code as in effect before the amendment made by subsection (a).

SEC. 243. REQUIRED DISTRIBUTIONS IN CASE OF INDIVIDUAL RETIREMENT PLANS.

(a) REQUIRED DISTRIBUTIONS AFTER DEATH.—

(1) INDIVIDUAL RETIREMENT ACCOUNTS.—Paragraph (7) of section 408(a) (defining individual retirement account) is amended to read as follows:

"(7) If—

"(A) an individual for whose benefit the trust is maintained dies before his entire interest has been distributed to him, or

"(B) distribution has been commenced as provided in paragraph (6) to his surviving spouse and such surviving spouse dies before the entire interest has been distributed to such spouse,

the entire interest (or the remaining part of such interest if distribution thereof has commenced) will be distributed within 5 years after his death (or the death of the surviving spouse). The preceding sentence shall not apply if distributions over a term certain commenced before the death of the individual for whose benefit the trust was maintained and the term certain is for a period permitted under paragraph (6)."

(2) INDIVIDUAL RETIREMENT ANNUITIES.—Paragraph (4) of section 408(b) (defining individual retirement annuity) is amended to read as follows:

"(4) If—

"(A) the owner dies before his entire interest has been distributed to him, or

"(B) distribution has been commenced as provided in paragraph (3) to his surviving spouse and such surviving spouse dies before the entire interest has been distributed to such spouse,

the entire interest (or the remaining part of such interest if distribution thereof has commenced) will be distributed within 5 years after his death (or the death of his surviving spouse). The preceding sentence shall not apply if distributions over a term certain commenced before the death of the owner and the term certain is for a period permitted under paragraph (3)."

(b) TREATMENT OF INHERITED INDIVIDUAL RETIREMENT PLANS.—

(1) DENIAL OF ROLLOVER TREATMENT.—

(A) Paragraph (3) of section 408(d) (defining rollover contributions) is amended by adding at the end thereof the following new subparagraph:

"(C) DENIAL OF ROLLOVER TREATMENT FOR INHERITED ACCOUNTS, ETC.—

"(i) In general.—In the case of an inherited individual retirement account or individual retirement annuity—

"(I) this paragraph shall not apply to any amount received by an individual from such an account or annuity (and no amount transferred from such account or annuity to another individual retirement account or annuity shall be excluded from gross income by reason of such transfer), and

"(II) such inherited account or annuity shall not be treated as an individual retirement account or annuity for purposes of determining whether any other amount is a rollover contribution.

"(ii) Inherited individual retirement account or annuity.—An individual retirement account or individual retirement annuity shall be treated as inherited if—

"(I) the individual for whose benefit the account or annuity is maintained acquired such account by reason of the death of another individual, and

"(II) such individual was not the surviving spouse of such other individual."

(B) Subparagraph (C) of section 409(b)(3) (relating to rollover into an individual retirement account or annuity or a qualified plan) is amended by adding at the end thereof the following new sentence: "This subparagraph shall not apply to any retirement bond if such bond is acquired by the owner by reason of the death of another individual and the owner was not the surviving spouse of such other individual."

(2) Denial of deduction for contributions to inherited individual retirement accounts or annuities.—Subsection (d) of section 219 (relating to other limitations and restrictions) is amended by adding at the end thereof the following new paragraph:

"(4) Denial of deduction for amount contributed to inherited annuities or accounts.—No deduction shall be allowed under this section with respect to any amount paid to an inherited individual retirement account or individual retirement annuity (within the meaning of section 408(d)(3)(C)(ii))."

(c) Effective Dates.—

(1) Subsection (a).—The amendments made by subsection (a) shall apply in the case of individuals dying after December 31, 1983.

(2) Subsection (b).—The amendments made by subsection (b) shall apply to taxable years beginning after December 31, 1983.

SEC. 244. LIMITATION ON EXCLUSION FOR GROUP-TERM LIFE INSURANCE PURCHASED FOR EMPLOYEES.

(a) General Rule.—Section 79 (relating to group-term life insurance purchased for employees) is amended by adding at the end thereof the following new subsection:

"(d) NONDISCRIMINATION REQUIREMENTS.—

"(1) IN GENERAL.—In the case of a discriminatory group-term life insurance plan, paragraph (1) of subsection (a) shall not apply with respect to any key employee.

"(2) DISCRIMINATORY GROUP-TERM LIFE INSURANCE PLAN.—For purposes of this subsection, the term 'discriminatory group-term life insurance plan' means any plan of an employer for providing group-term life insurance unless—

"(A) the plan does not discriminate in favor of key employees as to eligibility to participate, and

"(B) the type and amount of benefits available under the plan do not discriminate in favor of participants who are key employees.

"(3) NONDISCRIMINATORY ELIGIBILITY CLASSIFICATION.—

"(A) IN GENERAL.—A plan does not meet requirements of subparagraph (A) of paragraph (2) unless—

"(i) such plan benefits 70 percent or more of all employees of the employer,

"(ii) at least 85 percent of all employees who are participants under the plan are not key employees,

"(iii) such plan benefits such employees as qualify under a classification set up by the employer and found by the Secretary not to be discriminatory in favor of key employees, or

"(iv) in the case of a plan which is part of a cafeteria plan, the requirements of section 125 are met

"(B) EXCLUSION OF CERTAIN EMPLOYEES.—For purposes of subparagraph (A), there may be excluded from consideration—

"(i) employees who have not completed 3 years of service;

"(ii) part-time or seasonal employees;

"(iii) employees not included in the plan who are included in a unit of employees covered by an agreement between employee representatives and one or more employers which the Secretary finds to be a collective bargaining agreement, if the benefits provided under the plan were the subject of good faith bargaining between such employee representatives and such employer or employers; and

"(iv) employees who are nonresident aliens and who receive no earned income (within the meaning of section 911(d)(2)) from the employer which constitutes income from sources within the United States (within the meaning of section 861(a)(3)).

"(4) NONDISCRIMINATORY BENEFITS.—A plan does not meet the requirements of paragraph (2)(B) unless all benefits available to participants who are key employees are available to all other participants.

"(5) SPECIAL RULE.—A plan shall not fail to meet the requirements of paragraph (2)(B) merely because the amount of life insurance on behalf of the employees under the plan bears a uniform relationship to the total compensation or the basic or regular rate of compensation of such employees.

"(6) KEY EMPLOYEE DEFINED.—For purposes of this subsection, the term 'key employee' has the meaning given to such term by paragraph (1) of section 416(i), except that subparagraph (A)(iv) of such paragraph shall be applied by not taking into account employees described in paragraph (3)(B) who are not participants in the plan.

"(7) CERTAIN CONTROLLED GROUPS, ETC.—All employees who are treated as employed by a single employer under subsection (b), (c), or (m) of section 414 shall be treated as employed by a single employer for purposes of this section."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1983.

SEC. 245. LIMITATION ON ESTATE TAX EXCLUSIONS UNDER SECTION 2039.

(a) GENERAL RULE.—Section 2039 (relating to annuities) is amended by adding at the end thereof the following new subsection:

"(g) $100,000 LIMITATION ON EXCLUSIONS UNDER SUBSECTIONS (c) AND (e).—The aggregate amount excluded from the gross estate of any decedent under subsections (c) and (e) of this section shall not exceed $100,000."

(b) TECHNICAL AMENDMENTS.—Subsections (c) and (e) of section 2039 are each amended by striking out "Notwithstanding the provisions of this section" and inserting in lieu thereof "Subject to the limitation of subsection (g), notwithstanding any other provision of this section".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to the estates of decedents dying after December 31, 1982.

SEC. 246. ORGANIZATIONS PERFORMING MANAGEMENT FUNCTIONS.

(a) GENERAL RULE.—Subsection (m) of section 414 (relating to employees of an affiliated service group) is amended by redesignating paragraphs (5) and (6) as paragraphs (6) and (7), respectively, and by inserting after paragraph (4) the following new paragraph:

"(5) CERTAIN ORGANIZATIONS PERFORMING MANAGEMENT FUNCTIONS.—For purposes of this subsection, the term 'affiliated service group' also includes a group consisting of—

"(A) an organization the principal business of which is performing, on a regular and continuing basis, management functions for 1 organization (or for 1 organization and other organizations related to such 1 organization), and

"(B) the organization (and related organizations) for which such functions are so performed by the organization described in subparagraph (A).

For purposes of this paragraph, the term 'related organizations' has the same meaning as the term 'related persons' when used in section 103(b)(6)(C)."

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply to taxable years beginning after December 31, 1983.

SEC. 247. EXISTING PERSONAL SERVICE CORPORATIONS MAY LIQUIDATE UNDER SECTION 333 DURING 1983 OR 1984.

(a) IN GENERAL.—In the case of a complete liquidation of a personal service corporation (within the meaning of section 535(c)(2)(B) of the Internal Revenue Code of 1954) during 1983 or 1984, the fol-

lowing rules shall apply with respect to any shareholder other than a corporation:

(1) The determination of whether section 333 of such Code applies shall be made without regard to whether the corporation is a collapsible corporation to which section 341(a) of such Code applies.

(2) No gain or loss shall be recognized by the liquidating corporation on the distribution of any unrealized receivable in such liquidation.

(3)(A) Except as provided in subparagraph (C), any disposition by a shareholder of any unrealized receivable received in the liquidation shall be treated as a sale at fair market value of such receivable and any gain or loss shall be treated as ordinary gain or loss.

(B) For purposes of subparagraph (A), the term "disposition" includes—

"(i) failing to hold the property in the trade or business which generated the receivables, and

"(ii) failing to hold a continuing interest in such trade or business.

(C) For purposes of subparagraph (A), the term "disposition" does not include transmission at death to the estate of the decedent or transfer to a person pursuant to the right of such person to receive such property by reason of the death of the decedent or by bequest, devise, or inheritance from the decedent.

(4) Unrealized receivables distributed in the liquidation shall be treated as having a zero basis.

(5) For purposes of computing earnings and profits, the liquidating corporation shall not treat unrealized receivables distributed in the liquidation as an item of income.

(b) UNREALIZED RECEIVABLES DEFINED.—For purposes of this section, the term "unrealized receivables" has the meaning given such term by the first sentence of section 751(c) of such Code.

SEC. 248 EMPLOYEE LEASING.

(a) GENERAL RULE.—Section 414 (relating to definitions and special rules) is amended by adding at the end thereof the following new subsection:

"(n) EMPLOYEE LEASING.—

"(1) IN GENERAL.—For purposes of the pension requirements listed in paragraph (3), except to the extent otherwise provided in regulations, with respect to any person (hereinafter in this subsection referred to as the 'recipient') for whom a leased employee performs services—

"(A) the leased employee shall be treated as an employee of the recipient, but

"(B) contributions or benefits provided by the leasing organization which are attributable to services performed for the recipient shall be treated as provided by the recipient.

"(2) LEASED EMPLOYEE.—For purposes of paragraph (1), the term 'leased employee' means any person who provides services to the recipient if—

"(A) such services are provided pursuant to an agreement between the recipient and any other person (in this subsection referred to as the 'leasing organization'),

"(B) such person has performed such services for the recipient (or for the recipient and related persons) on a substantially full-time basis for a period of a least 1 year, and

"(C) such services are of a type historically performed, in the business field of the recipient, by employees.

"(3) PENSION REQUIREMENTS.—For purposes of this subsection, the pension requirements listed in this paragraph are—

"(A) paragraphs (3), (4), (7), and (16) of section 401(a), and

"(B) sections 408(k), 410, 411, 415, and 416.

"(4) TIME WHEN LEASED EMPLOYEE IS FIRST CONSIDERED AS EMPLOYEE.—In the case of any leased employee, paragraph (1) shall apply only for purposes of determining whether the pension requirements listed in paragraph (3) are met for periods after the close of the 1-year period referred to in paragraph (2); except that years of service for the recipient shall be determined by taking into account the entire period for which the leased employee performed services for the recipient (or related persons).

"(5) SAFE HARBOR.—This subsection shall not apply to any leased employee if such employee is covered by a plan which is maintained by the leasing organization if, with respect to such employee, such plan—

"(A) is a money purchase pension plan with a nonintegrated employer contribution rate of at least 7½ percent, and

"(B) provides for immediate participation and for full and immediate vesting.

"(6) RELATED PERSONS.—For purposes of this subsection, the term 'related persons' has the same meaning as when used in section 103(b)(6)(C)."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1983.

SEC. 249. NONDISCRIMINATORY COORDINATION OF DEFINED CONTRIBUTION PLANS WITH OASDI.

(a) IN GENERAL.—Section 401 (relating to qualified pension, profit-sharing, stock bonus plans, etc.) is amended by redesignating subsection (l) as subsection (o), and by inserting after subsection (k) the following new subsection:

"(l) NONDISCRIMINATORY COORDINATION OF DEFINED CONTRIBUTION PLANS WITH OASDI.—

"(1) IN GENERAL.—Notwithstanding subsection (a)(5), the coordination of a defined contribution plan with OASDI meets the requirements of subsection (a)(4) only if the total contributions with respect to each participant, when increased by the OASDI contributions, bear a uniform relationship—

"(A) to the total compensation of such employee, or

"(B) to the basic or regular rate of compensation of such employee.

"(2) DEFINITIONS.—For purposes of paragraph (1)—

"(A) OASDI CONTRIBUTIONS.—The term 'OASDI contributions' means the product of—

"(i) so much of the remuneration paid by the employer to the employee during the plan year as—

"(I) constitutes wages (within the meaning of section 3121(a) without regard to paragraph (1) thereof), and

"(II) does not exceed the contribution and benefit base applicable under OASDI at the beginning of the plan year, multiplied by

"(ii) the rate of tax applicable under section 3111(a) (relating to employer's OASDI tax) at the beginning of the plan year.

In the case of an individual who is an employee within the meaning of subsection (c)(1), the preceding sentence shall be applied by taking into account his earned income (as defined in subsection (c)(2)).

"(B) OASDI.—The term 'OASDI' means the system of old-age, survivors, and disability insurance established under title II of the Social Security Act and the Federal Insurance Contributions Act.

"(C) REMUNERATION.—The term 'remuneration' means—

"(i) total compensation, or

"(ii) basic or regular rate of compensation,

whichever is used in determining contributions or benefits under the plan.

"(3) DETERMINATION OF COMPENSATION, ETC., OF SELF-EMPLOYED INDIVIDUALS.—For purposes of this subsection, in the case of an individual who is an employee within the meaning of subsection (c)(1)—

"(A) his total compensation shall include his earned income (as defined in subsection (c)(2)), and

"(B) his basic or regular rate of compensation shall be determined (under regulations prescribed by the Secretary) with respect to that portion of his earned income which bears the same ratio to his earned income as the basic or regular compensation of the employees under the plan (other than employees within the meaning of subsection (c)(1)) bears to the total compensation of such employees."

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to plan years beginning after December 31, 1983.

SEC. 250. AUTHORITY OF SECRETARY TO ALLOCATE INCOME AND DEDUCTIONS IN THE CASE OF CERTAIN CORPORATIONS.

(a) IN GENERAL.—Part IX of subchapter B of chapter 1 (relating to items not deductible) is amended by adding after section 269 the following new section:

"SEC. 269A. PERSONAL SERVICE CORPORATIONS FORMED OR AVAILED OF TO AVOID OR EVADE INCOME TAX.

"(a) GENERAL RULE.—If—

"(1) substantially all of the services of a personal service corporation are performed for (or on behalf of) 1 other corporation, partnership, or other entity, and

"(2) the principal purpose for forming, or availing of, such personal service corporation is the avoidance or evasion of Federal income tax by reducing the income of, or securing the benefit of any expense, deduction, credit, exclusion, or other allowance for, any employee-owner which would not otherwise be available,

then the Secretary may allocate all income, deductions, credits, exclusions, and other allowances between such personal service corporation and its employee-owners, if such allocation is necessary to prevent avoidance or evasion of Federal income tax or clearly to reflect the income of the personal service corporation or any of its employee-owners.

"(b) DEFINITIONS.—For purposes of this section—

"(1) Personal service corporation.—The term 'personal service corporation' means a corporation the principal activity of which is the performance of personal services and such services are substantially performed by employee-owners.

"(2) EMPLOYEE-OWNER.—The term 'employee-owner' means any employee who owns, on any day during the taxable year, more than 10 percent of the outstanding stock of the personal service corporation. For purposes of the preceding sentence, section 318 shall apply, except that '5 percent' shall be substituted for '50 percent' in section 318(a)(2)(C).

"(3) RELATED PERSONS.—All related persons (within the meaning of section 106(b)(6)(C)) shall be treated as 1 entity."

(b) CLERICAL AMENDMENT.—The table of sections for part IX of subchapter 1 is amended by inserting after the item relating to section 269 the following new item:

"Sec. 269A. Personal service corporations formed or availed of to avoid or evade income tax."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1982.

PART IV—MISCELLANEOUS

SEC. 251. CHURCH PLANS.

(a) EXCLUSION ALLOWANCE.—

(1) ELECTION TO HAVE SECTION 415 RULES APPLY.—Subparagraph (B) of section 403(b)(2) (relating to exclusion allowance) is amended by striking out "(under section 415)" and inserting in lieu thereof "(under section 415 without regard to section 415(c)(8))".

(2) YEARS OF SERVICE.—Section 403(b)(2) is amended by adding at the end thereof the following new subparagraphs:

"(C) NUMBER OF YEARS OF SERVICE FOR DULY ORDAINED, COMMISSIONED, OR LICENSED MINISTERS OR LAY EMPLOYEES.—For purposes of this subsection and section 415(c)(4)(A)—

"(i) all years of service by—

"(I) a duly ordained, commissioned, or licensed minister of a church, or

"(II) a lay person,

as an employee of a church, a convention or association of churches, including an organization described in section 414(e)(3)(B)(ii), shall be considered as years of service for 1 employer, and

"(ii) all amounts contributed for annuity contracts by each such church (or convention or association of churches) or such organization during such years for such minister or lay person shall be considered to have been contributed by 1 employer.

For purposes of the preceding sentence, the terms 'church' and 'convention or association of churches' have the same meaning as when used in section 414(e).

"(D) ALTERNATIVE EXCLUSION ALLOWANCE.—

"(i) IN GENERAL.—In the case of any individual described in subparagraph (C), the amount determined under subparagraph (A) shall not be less than the lesser of—

"(I) $3,000, or

"(II) the includible compensation of such individual.

"(ii) SUBPARAGRAPH NOT TO APPLY TO INDIVIDUALS WITH ADJUSTED GROSS INCOME OVER $17,000.—This subparagraph shall not apply with respect to any taxable year to any individual whose adjusted gross income for such taxable year (determined separately and without regard to any community property laws) exceeds $17,000.

"(iii) SPECIAL RULE FOR FOREIGN MISSIONARIES.—In the case of an individual described in subparagraph (C)(i) performing services outside the United States, there shall be included as includible compensation for any year under clause (i)(II) any amount contributed during such year by a church (or convention or association of churches) for an annuity contract with respect to such individual."

(b) RETIREMENT INCOME ACCOUNTS PROVIDED BY CHURCHES, ETC.—Section 403(b) is amended by adding at the end thereof the following new paragraph:

"(9) RETIREMENT INCOME ACCOUNTS PROVIDED BY CHURCHES, ETC.—

"(A) AMOUNTS PAID TREATED AS CONTRIBUTIONS.—For purposes of this title—

"(i) a retirement income account shall be treated as an annuity contract described in this subsection, and

"(ii) amounts paid by an employer described in paragraph (1)(A) to a retirement income account shall be treated as amounts contributed by the employer for an annuity contract for the employee on whose behalf such account is maintained.

"(B) RETIREMENT INCOME ACCOUNT.—For purposes of this paragraph, the term 'retirement income account' means a defined contribution program established or maintained by a church, a convention or association of churches, including an organization described in section 414(e)(3)(A), to pro-

vide benefits under section 403(b) for an employee described in paragraph (1) or his beneficiaries."

(c) CONTRIBUTION LIMITATIONS.—

(1) APPLICATION OF SECTION 415(c)(4) TO CHURCH PLANS.—Paragraph (4) of section 415(c) (relating to special election for section 403(b) contracts) is amended—

(A) by striking out "or a home health service agency" each place it appears and inserting in lieu thereof "a home health service agency, or a church, convention or association of churches, or an organization described in section 414(e)(3)(B)(ii)",

(B) by inserting "(as determined for purposes of section 403(b)(2))" after "service for the employer" in subparagraph (A),

(C) by adding at the end of subparagraph (D) the following new clause:

"(iv) For purposes of this paragraph, the terms 'church' and 'convention or association of churches' have the same meaning as when used in section 414(e).", and

(D) by striking out "AND HOME HEALTH SERVICE AGENCIES" in the heading and inserting in lieu thereof ", HOME HEALTH SERVICE AGENCIES, AND CERTAIN CHURCHES, ETC.".

(2) TOTAL ANNUAL ADDITIONS.—Section 415(c) (relating to limitation on defined contribution plan) is amended by adding at the end thereof the following paragraph:

"(8) CERTAIN CONTRIBUTIONS BY CHURCH PLANS NOT TREATED AS EXCEEDING LIMITS.—

"(A) ALTERNATIVE EXCLUSION ALLOWANCE.—Any contribution or addition with respect to any participant, when expressed as an annual addition, which is allocable to the application of section 403(b)(2)(D) to such participant for such year, shall be treated as not exceeding the limitations of paragraph (1).

"(B) CONTRIBUTIONS NOT IN EXCESS OF $40,000 ($10,000 PER YEAR).—

"(i) IN GENERAL.—Notwithstanding any other provision of this subsection, at the election of a participant who is an employee of a church, a convention or association of churches, including an organization described in section 414(e)(3)(B)(ii), contributions and other additions for an annuity contract or retirement income account described in section 403(b) with respect to such participant, when expressed as an annual addition to such participant's account, shall be treated as not exceeding the limitation of paragraph (1) if such annual addition is not in excess of $10,000.

"(ii) $40,000 AGGREGATE LIMITATION.—The total amount of additions with respect to any participant which may be taken into account for purposes of this subparagraph for all years may not exceed $40,000.

"(iii) NO ELECTION IF PARAGRAPH (4)(A) ELECTION MADE.—No election may be made under this subpara-

graph for any year if an election is made under paragraph (4)(A) for such year.

"(C) ANNUAL ADDITION.—For purposes of this paragraph, the term 'annual addition' has the meaning given such term by paragraph (2)."

(3) CONFORMING AMENDMENT.—Section 403(b)(2)(B) (relating to exclusion allowance) is amended by striking out "and home health service agencies" and inserting in lieu thereof "home health service agencies, and certain churches, etc."

(d) CORRECTION PERIOD FOR CHURCH PLANS.—A church plan (within the meaning of section 414(e) of the Internal Revenue Code of 1954) shall not be treated as not meeting the requirements of section 401 or 403 of such Code if—

(1) by reason of any change in any law, regulation, ruling, or otherwise such plan is required to be amended to meet such requirements, and

(2) such plan is so amended at the next earliest church convention or such other time as the Secretary of the Treasury or his delegate may prescribe.

(e) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section shall apply to taxable years beginning after December 31, 1981.

(2) RETIREMENT INCOME ACCOUNTS.—The amendments made by subsection (b) shall apply to taxable years beginning after December 31, 1974.

(3) SECTION 415 AMENDMENTS.—The amendments made by subsection (c) shall apply to years beginning after December 31, 1981.

(4) CORRECTION PERIOD.—The amendment made by subsection (d) shall take effect on July 1, 1982.

(5) SPECIAL RULE FOR EXISTING DEFINED BENEFIT ARRANGEMENTS.—Any defined benefit arrangement which is established by a church or a convention or association of churches (including an organization described in section 414(e)(3)(B)(ii) of the Internal Revenue Code of 1954) and which is in effect on the date of the enactment of this Act shall not be treated as failing to meet the requirements of section 403(b)(2) of such Code merely because it is a defined benefit arrangement.

SEC. 252. DEFERRED COMPENSATION PLANS FOR STATE JUDGES.

Subsection (c) of section 131 of the Revenue Act of 1978 is amended by adding at the end thereof the following new paragraph:

"(3) DEFERRED COMPENSATION PLANS FOR STATE JUDGES.—

"(A) IN GENERAL.—The amendments made by this section shall not apply to any qualified State judicial plan.

"(B) QUALIFIED STATE JUDICIAL PLAN.—For purposes of subparagraph (A), the term 'qualified State judicial plan' means any retirement plan of a State for the exclusive benefit of judges or their beneficiaries if—

"(i) such plan has been continuously in existence since December 31, 1978,

"(ii) under such plan, all judges eligible to benefit under the plan—

"(I) are required to participate, and

"(II) are required to contribute the same fixed percentage of their basic or regular rate of compensation as judge,

"(iii) under such plan, no judge has an option as to contributions or benefits the exercise of which would affect the amount of includible compensation,

"(iv) the retirement payments of a judge under the plan are a percentage of the compensation of judges of that State holding similar positions, and

"(v) the plan during any year does not pay benefits with respect to any participant which exceed the limitations of section 415(b) of the Internal Revenue Code of 1954."

SEC. 253. PROFIT-SHARING PLAN CONTRIBUTIONS ON BEHALF OF DISABLED.

(a) IN GENERAL.—Paragraph (3) of section 415(c) (defining participant's compensation) is amended to read as follows:

"(3) PARTICIPANT'S COMPENSATION.—For purposes of paragraph (1)—

"(A) IN GENERAL.—The term 'participant's compensation' means the compensation of the participant from the employer for the year.

"(B) SPECIAL RULE FOR SELF-EMPLOYED INDIVIDUALS.—In the case of an employee within the meaning of section 401(c)(1), subparagraph (A) shall be applied by substituting 'the participant's earned income (within the meaning of section 401(c)(2) but determined without regard to any exclusion under section 911)' for 'compensation of the participant from the employer'.

"(C) SPECIAL RULES FOR PERMANENT AND TOTAL DISABILITY.—In the case of a participant—

"(i) who is permanently and totally disabled (as defined in section 105(d)(4)),

"(ii) who is not an officer, owner, or highly compensated, and

"(iii) with respect to whom the employer elects, at such time and in such manner as the Secretary may prescribe, to have this subparagraph apply,

the term 'participant's compensation' means the compensation the participant would have received for the year if the participant was paid at the rate of compensation paid immediately before becoming permanently and totally disabled. This subparagraph shall only apply if contributions made with respect to such participant are nonforfeitable when made."

(b) DEDUCTIBILITY.—Subparagraph (B) of section 404(a)(3) (relating to limits on deductible contributions to stock bonus and profit-sharing trusts) is amended by adding at the end thereof the following: "The term 'compensation otherwise paid or accrued during the taxable year to all employees' shall include any amount with respect to which an election under section 415(c)(3)(C) is in effect, but only

to the extent that any contribution with respect to such amount is nonforfeitable."

(c) Effective Date.—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

SEC. 254. EXEMPTION FOR TRUSTS WHICH INCLUDE GOVERNMENTAL PLANS.

(a) In General.—Section 401(a) (relating to requirements of qualification for qualified pension, profit-sharing, and stock bonus plans) is amended by inserting immediately after paragraph (23) the following new paragraph:

> *"(24) Any group trust which otherwise meets the requirements of this section shall not be treated as not meeting such requirements on account of the participation or inclusion in such trust of the moneys of any plan or governmental unit described in section 805(d)(6)."*

(b) Effective Date.—The amendment made by subsection (a) shall apply with respect to taxable years beginning after December 31, 1981.

Subtitle D—Taxation of Life Insurance Companies and Annuities

PART I—COINSURANCE ARRANGEMENTS

Subpart A—Modified Coinsurance Contracts

SEC. 255. REPEAL OF OPTIONAL TREATMENT OF POLICIES REINSURED UNDER MODIFIED COINSURANCE CONTRACTS.

(a) Repeal of Section 820.—Section 820 (relating to optional treatment of policies reinsured under modified coinsurance contracts) is repealed.

(b) Conforming Amendments.—

> *(1) Section 811 (relating to dividends to policyholders) is amended by adding at the end thereof the following new subsection:*

"(c) Special Rule for Dividends to Policyholders Under Reinsurance Contracts.—If, under the terms of a conventional coinsurance contract, a life insurance company (hereinafter referred to as 'the reinsurer') is obligated to reimburse another life insurance company (hereinafter referred to as 'the reinsured') for dividends to policyholders on the policies reinsured, the amount of the deduction for dividends reimbursed shall, for purposes of section 809(d)(12), be equal to the amount of dividends to policyholders—

> *"(1) which were paid by the reinsured, and*
>
> *"(2) with respect to which the reinsurer reimbursed the reinsured under the terms of such contract.*

The amount determined under the preceding sentence shall be properly adjusted to reflect the adjustments under subsection (b)(1)."

> *(2) The first sentence of section 809(c)(1) (relating to premiums) is amended to read as follows: "The gross amount of premiums and other consideration, including—*
>
> > *"(A) advance premiums,*
> >
> > *"(B) deposits,*

"(C) fees,

"(D) assessments,

"(E) consideration in respect of assuming liabilities under contracts not issued by the taxpayer, and

"(F) the amount of dividends to policyholders reimbursed to the taxpayer by a reinsurer in respect of reinsured policies,

on insurance and annuity contracts (including contracts supplementary thereto); less return premiums, and premiums and other consideration arising out of reinsurance ceded."

(3) Section 809(d)(3) (relating to dividends to policyholders) is amended by inserting ", other than the deduction provided under paragraph (12)" before the period at the end thereof.

(4) Section 809(d) (relating to deductions in computing gain and loss from operations) is amended by adding after paragraph (11) thereof the following new paragraph:

"(12) DIVIDENDS REIMBURSED.—The deduction for the amount of dividends to policyholders reimbursed by the taxpayer to another insurance company in respect of policies the taxpayer has reinsured (determined under section 811(c))."

(5) The table of sections for subpart E of part I of subchapter L of chapter 1 is amended by striking out the item relating to section 820.

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to taxable years beginning after December 31, 1981.

(2) RULES APPLICABLE TO TAXABLE YEARS BEGINNING BEFORE JANUARY 1, 1982.—

(A) IN GENERAL.—In the case of any taxable year beginning before January 1, 1982—

(i) any determination as to whether any contract met the requirements of subsection (b) of section 820 of the Internal Revenue Code of 1954 (as in effect before its repeal by this section) shall be made solely by reference to the terms of the contract, and

(ii) the treatment of such contract under subsection (c) of such section 820 shall be made in accordance with the regulations under such section which were in effect on December 31, 1981.

(B) PARAGRAPH NOT TO APPLY IF FRAUD INVOLVED.—The provisions of subparagraph (A) shall not apply with respect to any deficiency which the Secretary of the Treasury or his delegate establishes was due to fraud with intent to evade tax.

SEC. 256. SPECIAL ACCOUNTING RULES RELATING TO REPEAL OF SECTION 820.

(a) IN GENERAL.—For purposes of subchapter L of chapter 1 of the Internal Revenue Code of 1954, the provisions of this section shall apply to any contract—

(1) which was in effect on December 31, 1981, and

(2) to which section 820(a)(1) of such Code (as in effect before its repeal by section 255(a)) applied.

(b) Treatment of Reserves and Assets.—Except as provided in subsections (c) and (d), the reserves on the contract described in subsection (a) and the assets in relation to such reserves shall—

(1) as of the beginning of taxable year 1982, be treated as the reserves and assets of the reinsurer (and not the reinsured), and

(2) as of the end of taxable year 1982, be treated as the reserves and assets of the reinsured (and not the reinsurer).

(c) Allocation of Certain Section 820(c) Items.—Any amount described in paragraphs (1), (2), (4), and (5) of section 820(c) of such Code (as so in effect) with respect to any contract described in subsection (a) shall, beginning with taxable year 1982, be taken into account by the reinsured and the reinsurer in the same manner as such amounts would be taken into account under a modified coinsurance contract to which section 820(a)(1) of such Code (as so in effect) does not apply.

(d) Amounts Treated as Returned Under the Contract.—

(1) In general.—For taxable year 1982—

(A) in the case of the reinsurer, there shall be allowed as a deduction for ordinary and necessary business expenses under section 809(d)(11) of such Code an amount equal to the termination amount (and such amount shall not otherwise be taken into account in determining gain or loss from operations under section 809 of such Code), and

(B) in the case of the reinsured, the gross amount under section 809(c)(3) of such Code shall be increased by the termination amount.

(2) Adjustment for reserves of reinsured.—For purposes of subsections (a) and (b) of section 810 of such Code, the amount taken into account as of the close of taxable year 1982 by the reinsured shall be reduced for such taxable year (but not for purposes of determining such amount at the beginning of the next succeeding taxable year) by the excess (if any) of—

(A) the reserves on the contract as of January 1, 1982 (determined under the reinsured's method of computing reserves for tax purposes), over

(B) the termination amount.

This paragraph shall not apply to any portion of any policies with respect to which the taxpayer is both the reinsured and the reinsurer under contracts to which this section applies.

(3) Termination amount.—For purposes of this subsection, the term "termination amount" means the amount under the contract, the reinsurer would have returned to the reinsured upon termination of the contract if the contract had been terminated as of January 1, 1982.

(4) Certain amounts not taken into account under section 809(d)(5).—Any amount treated as the reserves of the reinsured by reason of subsection (b)(2) shall not be taken into account under section 809(d)(5) of the Internal Revenue Code of 1954.

(e) 3-Year Installment Payment of Taxes Owed by Reinsurer Resulting From Repeal of Section 820.—

(1) In general.—That portion of any tax imposed under chapter 1 of such Code (reduced by the sum of the credits allowable under subpart A of part IV of such chapter) on a reinsurer

for taxable year 1982 which is attributable to the excess (if any) of—

(A) any decrease in reserves for such taxable year by reason of subsection (b), over

(B) the amount allowable as a deduction for such taxable year by reason of subsection (d)(1)(A),

may, at the election of the reinsurer, be paid in 3 equal annual installments.

(2) TIME FOR PAYMENTS.—

(A) IN GENERAL.—The 3 installments under paragraph (1) shall be paid on March 15 of 1983, 1984, and 1985.

(B) FIRST INSTALLMENT MAY BE MADE IN 2 PAYMENTS.—The reinsurer may elect to pay one-half of the installment due March 15, 1983, on June 15, 1983.

(3) ACCELERATION OF PAYMENTS.—If—

(A) an election is made under paragraph (1), and

(B) before the tax attributable to such excess is paid in full any installment under this section is not paid on or before the date fixed by this section for its payment,

then the extension of time for payment of tax provided in this subsection shall cease to apply, and any portion of the tax payable in installments shall be paid on notice and demand from the Secretary of the Treasury or his delegate.

(4) PRORATION OF DEFICIENCY TO INSTALLMENTS.—If an election is made under paragraph (1) and a deficiency attributable to the excess has been assessed, the deficiency shall be prorated to such installments. The part of the deficiency so prorated to any installment the date for payment of which has not arrived shall be collected at the same time as, and as part of, such installment. The part of the deficiency so prorated to any installment the date for payment of which has arrived shall be paid on notice and demand from the Secretary of the Treasury or his delegate. This paragraph shall not apply if the deficiency is due to negligence, to intentional disregard of rules and regulations, or to fraud with intent to evade tax.

(5) BOND MAY BE REQUIRED.—If an election is made under this section, section 6165 of the Internal Revenue Code of 1954 shall apply as though the Secretary of the Treasury or his delegate were extending the time for payment of the tax.

(6) EXTENSION OF PERIOD OF LIMITATIONS.—The running of any period of limitations for the collection of the tax with respect to which an election is made under paragraph (1) shall be suspended for the period during which there are any unpaid installments of such tax.

(7) INTEREST ON INSTALLMENTS.—Rules similar to the rules of section 6601(b)(2) of such Code (without regard to the last sentence thereof) shall apply with respect to any tax for which an election is made under paragraph (1).

(f) SPECIAL RULE ALLOWING REINSURED TO REVOKE AN ELECTION UNDER SECTION 820.—

(1) IN GENERAL.—In any case in which—

(A) a taxpayer is the reinsured under any contract—

(i) which took effect in 1980 or 1981, and

(ii) with respect to which an election under section 820 of the Internal Revenue Code of 1954 was made,

(B) the taxpayer has a loss from operations or its gain from operations (determined without regard to any deduction under paragraphs (3), (5), and (6) of section 809(d) of such Code) for the taxable year in which such contract took effect does not exceed the taxpayer's taxable investment income for such taxable year,

(C) such contract was not a contract with a person who, during the taxable year in which such contract took effect, was a member of the same affiliated group (determined under section 1504 of such Code without regard to subsection (b)) of which the taxpayer is a member, and

(D) the taxpayer makes an election under this subsection within 6 months after the date of the enactment of this Act,

then the provisions of paragraph (2) shall apply.

(2) RULES WHICH APPLY IF THIS SUBSECTION APPLIES.—In any case described in paragraph (1)—

(A) the taxpayer shall, for all taxable years, be treated as not having made an election under section 820 of such Code with respect to the contract described in paragraph (1), but

(B) all other parties to the contract shall be treated as having made such election with respect to such contract for all taxable years.

(g) TAXABLE YEAR 1982.—For purposes of this section, the term "taxable year 1982" means, with respect to any taxpayer, the first taxable year of the taxpayer beginning after December 31, 1981.

(h) REGULATIONS.—The Secretary of the Treasury or his delegate shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section.

Subpart B—Other Reinsurance Agreements

SEC. 257. DENIAL OF INTEREST DEDUCTION ON INDEBTEDNESS INCURRED IN CONNECTION WITH REINSURANCE AGREEMENTS.

(a) IN GENERAL.—Section 805(e) (relating to interest paid) is amended by adding at the end thereof the following new sentence: "For purposes of this subpart, the interest paid for any taxable year shall not include any interest paid or accrued after December 31, 1981, by a ceding company (or its affiliates) to any person in connection with a reinsurance agreement (other than interest on account of delay in making periodic settlements of income and expense items under the terms of the agreement)."

(b) SPECIAL TRANSITIONAL RULE WHERE AT LEAST 20 PERCENT OF THE LIABILITIES REINSURED ARE PAID IN CASH, ETC.—The amendment made by subsection (a) shall not apply with respect to any interest paid or incurred by a ceding company to a person who is a member of the same affiliated group (within the meaning of section 1504 of the Internal Revenue Code of 1954) on indebtedness evidenced by a note—

(1) which was entered into after December 31, 1981, with respect to a reinsurance contract under the terms of which an amount not less than 20 percent of the amounts reinsured was

paid in cash to the reinsurer on the effective date of such contract,

(2) at least 40 percent of the principal of which had been paid by the ceding company in cash as of July 1, 1982, and

(3) the remaining balance of which is paid in cash before January 1, 1983.

SEC. 258. ALLOCATION OF INCOME, ETC. IN THE CASE OF OTHER REINSURANCE AGREEMENTS.

(a) In General.—Section 818 (relating to accounting provisions) is amended by adding at the end thereof the following new subsection:

"(g) Allocation in Case of Reinsurance Agreement Involving Tax Avoidance or Evasion.—In the case of 2 or more related persons (within the meaning of section 1239(b)) who are parties to a reinsurance agreement, the Secretary may—

"(1) allocate between or among such persons income (whether investment income, premium, or otherwise), deductions, assets, reserves, credits, and other items related to such agreement, or

"(2) recharacterize any such items,

if he determines that such allocation or recharacterization is necessary to reflect the proper source and character of the taxable income (or any item described in paragraph (1) relating to such taxable income) of each such person.".

(b) Effective Date.—The amendment made by subsection (a) shall apply to agreements entered into after the date of the enactment of this Act.

PART II—2-YEAR TEMPORARY PROVISIONS RELATING TO TAXATION OF LIFE INSURANCE COMPANIES

SEC. 259. INCREASE IN AMOUNT OF DIVIDEND DEDUCTION ALLOWED; PENSION PLAN RESERVES.

(a) Increase in Limitation.—Section 809(f) (relating to limitation on certain deductions) is amended to read as follows:

"(f) Limitation on Certain Deductions.—

"(1) In general.—The amount of the deductions under paragraphs (3), (5), and (6) of subsection (d) shall not exceed the greater of—

"(A) $1,000,000, plus the amount (if any) by which—

"(i) the gain from operations for the taxable year (computed without regard to such deductions), exceeds

"(ii) the taxable investment income for the taxable year, or

"(B) if the taxpayer elects for any taxable year, the amount determined under paragraph (2).

"(2) Alternative limitation.—The amount determined under this paragraph for any taxable year shall be equal to the sum of—

"(A) that portion of the deduction under subsection (d)(3) which is allocable to any contract described in section 805(d), and

"(B) an amount equal to the sum of—

"(i) so much of the base amount as does not exceed $1,000,000, plus

"(ii) in the case of—

"(I) a mutual life insurance company, 77.5 percent of the base amount, or

"(II) a stock life insurance company, 85 percent of the base amount.

"(3) Reduction in $1,000,000 amount for large insurers.—If the sum of the deductions under paragraphs (3), (5), and (6) of subsection (d) exceeds $4,000,000, then each of the $1,000,000 amounts in paragraphs (1) and (2) shall be reduced (but not below zero) by the amount which bears the same ratio to $1,000,000 as—

"(A) the amount of such excess bears to,

"(B) $4,000,000.

"(4) Base amount.—For purposes of paragraph (2)(B), the term 'base amount' means the excess of—

"(A) the amount of the deductions under paragraphs (3) and (5) of subsection (d) for the taxable year, over

"(B) the amount determined under paragraph (2)(A) for such taxable year.

"(5) Application of limitation.—The limitation provided by paragraph (1) shall apply first to the amount of the deduction under subsection (d)(3), then to the amount of the deduction under subsection (d)(5), and finally to the amount of the deduction under subsection (d)(6)."

(b) $1,000,000 Limitation To Be Apportioned Among Members of Same Controlled Group.—Section 1561(a) (relating to limitations on certain multiple tax benefits in the case of certain controlled corporations) is amended—

(1) by striking out "and" at the end of paragraph (2),

(2) by striking out the period at the end of paragraph (3) and inserting in lieu thereof a comma and "and",

(3) by inserting after paragraph (3) the following new paragraph:

"(4) one $1,000,000 amount (adjusted as provided in section 809(f)(3)) for purposes of computing the limitation under paragraph (1) or (2) of section 809(f).", and

(4) by striking out "(2) and (3)" and inserting in lieu thereof "(2), (3), and (4)".

(c) Conforming Amendments.—Section 1561(b) (relating to certain short taxable years) is amended—

(1) by striking out "and" at the end of paragraph (2),

(2) by striking out the comma at the end of paragraph (3) and inserting in lieu thereof a comma and "and",

(3) by inserting after paragraph (3) the following new paragraph:

"(4) the amount (adjusted as provided in section 809(f)(3)) to be used in computing the limitation under paragraph (1) or (2) of section 809(f),", and

(4) by striking out "(2), or (3)" and inserting in lieu thereof "(2), (3), or (4)".

SEC. 260. COMPUTATION OF AMOUNT OF LIFE INSURANCE RESERVES.

(a) Reserves on Contracts on Which Certain Interest Is Guaranteed Beyond the End of the Taxable Year.—Section 818 (relating to accounting provisions), as amended by section

259(a), is amended by adding at the end thereof the following new subsection:

"(h) METHOD OF COMPUTING RESERVES ON CONTRACT WHERE INTEREST IS GUARANTEED BEYOND END OF TAXABLE YEAR.—For purposes of this part (other than section 801), interest payable under any contract which is computed at a rate which—

"(1) is in excess of the lowest rates which are assumed under such contract for any period in calculating the reserves under section 810(c) for the contract under which such interest is payable, and

"(2) is guaranteed beyond the end of the taxable year on which the reserves are being computed,

shall be taken into account in computing the reserves with respect to such contract as if such interest were guaranteed only up to the end of the taxable year."

(b) PROHIBITION AGAINST DEDUCTION OF INTEREST IN EXCESS OF AMOUNT CREDITED TO GROUP PENSION POLICYHOLDERS.—Section 805 (relating to the determination of policy and other contract liability requirements) is amended by adding at the end thereof the following:

"(g) SPECIAL LIMITATION FOR GROUP PENSION CONTRACTS.—The amount determined under paragraphs (2) and (3) of subsection (a) for policy and other contract liability requirements for group pension contracts shall not exceed the amount actually credited to the policyholders whether such crediting is through premium rate computations, reserve increases, excess interest, experience rate credits, policyholder dividends or otherwise. The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subsection."

(c) PROHIBITION AGAINST CHANGING THE QUALIFICATION STATUS OF LIFE INSURANCE COMPANIES.—For any taxable year ending before January 1, 1984, a taxpayer shall not be treated as other than a life insurance company (as defined in section 801(a) of such Code) because of the effect of amounts held under contracts which would be described in section 805(d) of the Internal Revenue Code of 1954, except for the fact that such contracts do not contain permanent annuity purchase rate guarantees.

SEC. 261. MODIFICATION OF MENGE FORMULA.

Subparagraph (B) of section 805(c)(1) (defining adjusted life insurance reserves rate) is amended to read as follows:

"(B) 0.9 raised to the power of n where n is the number (positive or negative) determined by subtracting—

"(i) 100 times the average rate of interest assumed by the taxpayer in calculating such reserves, from

"(ii) 100 times the adjusted reserves rate."

SEC. 262. CONSOLIDATED RETURNS TO BE COMPUTED ON A BOTTOM LINE BASIS.

Subsection (f) of section 818 (relating to computation on consolidated returns of policyholders' share of investment yield) is amended to read as follows:

"(f) SPECIAL RULES FOR CONSOLIDATED RETURN COMPUTATIONS.—For purposes of this part, in the case of a life insurance company

filing or required to file a consolidated return under section 1501 for a taxable year the following rules shall apply:

"(1) POLICYHOLDERS' SHARE OF INVESTMENT YIELD.—The computation of the policyholders' share of investment yield under subparts B and C (including all determinations and computations incident thereto) shall be made as if such company were not filing a consolidated return.

"(2) LIFE INSURANCE COMPANY TAXABLE INCOME.—

"(A) IN GENERAL.—The amount of the consolidated life insurance company taxable income under paragraphs (1) and (2) of section 802(b) shall be determined by taking into account the life insurance company taxable income (including any case where deductions exceed income) of each life insurance company which is a member of the group (as computed separately under such paragraphs).

"(B) CERTAIN AMOUNTS COMPUTED SEPARATELY.—For purposes of subparagraph (A), the determination of a life insurance company's taxable investment income and gain or loss from operations (after applying the limitation provided by section 809(f)) shall be made without regard to the taxable investment income or gain or loss from operations of any other such company.

"(3) CONSOLIDATED NET CAPITAL GAIN.—If there is a consolidated net capital gain, then the partial tax referred to in section 802(a)(2)(A) shall be computed on—

"(A) the consolidated life insurance company taxable income, reduced (but not below the sum of the amounts determined under section 802(b)(3)) by

"(B) the amount of such consolidated net capital gain."

SEC. 263. EFFECTIVE DATES; SPECIAL RULES APPLICABLE TO TRANSACTIONS BEFORE EFFECTIVE DATE.

(a) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this part shall apply to taxable years beginning after December 31, 1981, and before January 1, 1984.

(2) GROUP PENSION CONTRACTS.—The amendments made by section 260(b) shall apply to taxable years beginning after December 31, 1982, and before January 1, 1984.

(3) RESERVES ON CONTRACTS WHERE INTEREST GUARANTEED FOR EXTENDED PERIODS.—

(A) IN GENERAL.—The amendment made by section 260(a) shall apply to reserves computed for taxable years beginning after December 31, 1981, and before January 1 1984, with respect to guarantees made after July 1, 1982, and before January 1, 1984.

(B) SPECIAL RULE RELATING TO RESERVES.—If, for any taxable year beginning before January 1, 1982—

(i) a taxpayer increased reserves pursuant to section 810(c)(4) of the Internal Revenue Code of 1954 to reflect interest guaranteed beyond the end of such taxable year, and *(ii) the Federal income tax liability of such taxpayer for all taxable years would be the same if such liability was computed with or without regard to such reserves,*

then such reserves shall, as of the beginning of the first taxable year of the taxpayer beginning after December 31, 1981, be recomputed as if section 818(h) of such Code (as added by this Act) applied to such reserves. If this subparagraph applies to any taxpayer, subparagraph (A) shall be applied with respect to such taxpayer by striking out "after July 1, 1982, and".

(b) SPECIAL RULES FOR CERTAIN TRANSACTIONS IN TAXABLE YEARS BEGINNING BEFORE JANUARY 1, 1982.—

(1) CERTAIN INTEREST AND PREMIUMS.—

(A) IN GENERAL.—In the case of any taxable year beginning before January 1, 1982, if a taxpayer, on his return of tax for such taxable year, treated—

(i) any amount described in subparagraph (B) as an amount which was not a dividend to policyholders (within the meaning of section 811 of the Internal Revenue Code of 1954), or

(ii) any amount described in subparagraph (C) as not described in section 809(c)(1),

then such amounts shall be so treated for purposes of the Internal Revenue Code of 1954.

(B) CERTAIN INTEREST.—An amount is described in this subparagraph if such amount is in the nature of interest accrued for the taxable year on an insurance or annuity contract pursuant to—

(i) an interest rate guaranteed or fixed before the period of payment of such amount begins, or

(ii) any other method (fixed before such period begins) the terms of which during the period are beyond the control and are independent of the experience of the company, whether or not the interest rate or other method was guaranteed or fixed for any specified period of time.

(C) AMOUNTS NOT TREATED AS PREMIUMS.—An amount is described in this subparagraph if such amount represents the difference between—

(i) the amount of premiums received or mortality charges made under rates fixed in advance of the premium or mortality charge due date, and

(ii) the maximum premium or mortality charge which could be charged under the terms of the insurance or annuity contract.

(D) NO INFERENCE.—The provisions of this paragraph shall constitute no inference with respect to the treatment of any item in taxable years beginning after December 31, 1981.

(2) CONSOLIDATED RETURNS.—The provisions of section 818(f) of such Code, as amended by section 262, shall apply to any taxable year beginning before January 1, 1982, if the taxpayer filed a consolidated return before July 1, 1982 for such taxable year under section 1501 of such Code which, on such date (deter-

mined without regard to any amended return filed after June 30, 1982), was consistent with the provisions of section 818(f) of such Code, as so amended. In the case of a taxable year beginning in 1981, the preceding sentence shall be applied by substituting "September 16" for "July 1" and "September 15" for "June 30".

(3) TAXABLE YEARS WHERE PERIOD OF LIMITATION HAS RUN.—This subsection shall not apply to any taxable year with respect to which the statute of limitations for filing a claim for credit or refund has expired under any provision of law or by operation of law.

PART III—EXCESS INTEREST; AMOUNTS RECEIVED UNDER ANNUITY CONTRACTS; FLEXIBLE PREMIUM CONTRACTS; COMPUTATION OF RESERVES

SEC. 264. ALLOWANCE OF DEDUCTION FOR EXCESS INTEREST.

(a) IN GENERAL.—Subsection (e) of section 805 (defining interest paid) is amended by adding at the end thereof the following new paragraph:

"(5) QUALIFIED GUARANTEED INTEREST.—Qualified guaranteed interest (within the meaning of subsection (f))".

(b) QUALIFIED GUARANTEED INTEREST DEFINED.—Section 805 (relating to policy and other contract liability requirements) is amended by adding at the end thereof the following new subsection:

"(f) QUALIFIED GUARANTEED INTEREST AND QUALIFIED CONTRACTS.—For purposes of this section—

"(1) IN GENERAL.—The term 'qualified guaranteed interest' means any amount in the nature of interest for the taxable year on qualified contracts, but only if such amount is determined pursuant to—

"(A) a stated rate of interest which is guaranteed—

"(i) before the beginning of the period for which the interest accrues, and

"(ii) for a period of not less than 12 months (or for a period ending not earlier than the close of the taxable year in which the contract was issued), or

"(B) a rate or rates of interest which—

"(i) meet the requirements of clause (i) of subparagraph (A), and

"(ii) is determined under a formula or other method the terms of which—

"(I) during the period referred to in subparagraph (A)(ii) may not be changed by the taxpayer, and

"(II) are independent of the experience of the taxpayer.

"(2) QUALIFIED CONTRACT.—The term 'qualified contract' means any annuity contract (other than any contract described in subsection (d)) which—

"(A) involves (at the time the qualified interest is credited under the contract) life contingencies,

"(B) provides no right under State law for the policyholder to participate in the divisible surplus of the taxpayer, and

"(C) provides that the taxpayer may from time to time credit amounts in the nature of interest in excess of amounts computed on the basis of any rate or rates guaranteed in the contract at the time it was entered into.

"(3) SPECIAL RULE FOR PARTICIPATING CONTRACTS.—

"(A) IN GENERAL.—In the case of an annuity contract which is not a qualified contract solely because it fails to satisfy the requirements of subparagraph (B) of paragraph (2), such contract shall be treated as a qualified contract and the amount taken into account as qualified guaranteed interest with respect to such contract shall be equal to the sum of—

"(i) the amount of interest which would be assumed in calculating reserves with respect to such contract under section 810(c) if such interest were not taken into account under subsection (e), plus

"(ii) 92.5 percent of the excess of—

"(I) the amount of qualified guaranteed interest (determined without regard to this paragraph and as if such contract were a qualified contract), over

"(II) the amount determined under clause (i).

"(B) INTEREST NOT OTHERWISE TAKEN INTO ACCOUNT.—No deduction shall be allowed under any other provision of this part for the 7.5 percent of the excess described in subparagraph (A)(ii) which is not treated as qualified guaranteed interest."

(c) CONFORMING AMENDMENTS.—

(1) Subparagraph (A) of section 805(c)(1) (defining adjusted life insurance reserves) is amended by inserting "or reserves on any qualified contract" after "pension plan reserves".

(2) Paragraph (2) of section 809(a) (defining required interest) is amended—

(A) by inserting "the amount of qualified guaranteed interest (within the meaning of section 805(f)(1)) and" after "the sum of"; and

(B) by adding at the end thereof the following new sentence:

"For purposes of subparagraphs (A) and (B), reserves on qualified contracts (within the meaning of section 805(f)(2)) shall not be taken into account."

(3) Paragraph (1) of section 809(e) (relating to modification of interest deduction) is amended by inserting "qualified guaranteed interest (within the meaning of section 805(f)(1) or" after "allowed for".

(d) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1981.

(2) GUARANTEES FOR LESS THAN 12 MONTHS.—

(A) MONEYS HELD BEFORE AUGUST 14, 1982.— The requirements of subparagraph (A)(ii) or (B)(ii)(I) of section 805(f)(1) of the Internal Revenue Code of 1954 (as added by subsec-

tion (b)) shall not apply to any moneys held under any contract on August 13, 1982 (and any interest on such moneys after such date).

(B) CONTRACTS ENTERED INTO AFTER AUGUST 13, 1982, AND BEFORE JANUARY 1, 1983.—A contract entered into after August 13, 1982, and before January 1, 1983, shall be treated as meeting the requirements of subparagraph (A)(ii) or (B)(ii)(I) of such Code if it meets such requirements on the first contract anniversary date.

SEC. 265. TREATMENT OF AMOUNTS RECEIVED UNDER ANNUITY CONTRACTS BEFORE ANNUITY STARTING DATE.

(a) IN GENERAL.—Subsection (e) of section 72 (relating to amounts not received as annuities) is amended to read as follows:

"(e) AMOUNTS NOT RECEIVED AS ANNUITIES.—

"(1) APPLICATION OF SUBSECTION.—

"(A) IN GENERAL.—This subsection shall apply to any amount which—

"(i) is received under an annuity, endowment, or life insurance contract, and

"(ii) is not received as an annuity,

if no provision of this subtitle (other than this subsection) applies with respect to such amount.

"(B) DIVIDENDS.—For purposes of this section, any amount received which is in the nature of a dividend or similar distribution shall be treated as an amount not received as an annuity.

"(2) GENERAL RULE.—Any amount to which this subsection applies—

"(A) if received on or after the annuity starting date, shall be included in gross income, or

"(B) if received before the annuity starting date—

"(i) shall be included in gross income to the extent allocable to income on the contract, and

"(ii) shall not be included in gross income to the extent allocable to the investment in the contract.

"(3) ALLOCATION OF AMOUNTS TO INCOME AND INVESTMENT.—For purposes of paragraph (2)(B)—

"(A) ALLOCATION TO INCOME.—Any amount to which this subsection applies shall be treated as allocable to income on the contract to the extent that such amount does not exceed the excess (if any) of—

"(i) the cash value of the contract (determined without regard to any surrender charge) immediately before the amount is received, over

"(ii) the investment in the contract at such time.

"(B) ALLOCATION TO INVESTMENT.—Any amount to which this subsection applies shall be treated as allocable to investment in the contract to the extent that such amount is not allocated to income under subparagraph (A).

"(4) SPECIAL RULES FOR APPLICATION OF PARAGRAPH (2)(B).—For purposes of paragraph (2)(B)—

"(A) LOANS TREATED AS DISTRIBUTIONS.—If, during any taxable year, an individual—

"(i) receives (directly or indirectly) any amount as a loan under any contract to which this subsection applies, or

"(ii) assigns or pledges (or agrees to assign or pledge) any portion of the value of any such contract,

such amount or portion shall be treated as received under the contract as an amount not received as an annuity.

"(B) TREATMENT OF POLICYHOLDER DIVIDENDS.—Any amount described in paragraph (1)(B) shall not be included in gross income under paragraph (2)(B)(i) to the extent such amount is retained by the insurer as a premium or other consideration paid for the contract.

"(5) RETENTION OF EXISTING RULES IN CERTAIN CASES.—

"(A) IN GENERAL.—In any case to which this paragraph applies—

"(i) paragraphs (2)(B) and (4)(A) shall not apply, and

"(ii) if paragraph (2)(A) does not apply,

the amount shall be included in gross income, but only to the extent it exceeds the investment in the contract.

"(B) EXISTING CONTRACTS.—This paragraph shall apply to contracts entered into before August 14, 1982. Any amount allocable to investment in the contract after August 13, 1982, shall be treated as from a contract entered into after such date.

"(C) CERTAIN LIFE INSURANCE AND ENDOWMENT CONTRACTS.—Except to the extent prescribed by the Secretary by regulations, this paragraph shall apply to any amount not received as an annuity which is received under a life insurance or endowment contract.

"(D) CONTRACTS UNDER QUALIFIED PLANS.—This paragraph shall apply to any amount received—

"(i) from a trust described in section 401(a) which is exempt from tax under section 501(a),

"(ii) from a contract—

"(I) purchased by a trust described in clause (i),

"(II) purchased as part of a plan described in section 403(a),

"(III) described in section 403(b), or

"(IV) provided for employees of a life insurance company under a plan described in section 805(d)(3), or

"(iii) from an individual retirement account or an individual retirement annuity.

"(E) FULL REFUNDS, SURRENDERS, REDEMPTIONS, AND MATURITIES.—This paragraph shall apply to—

"(i) any amount received, whether in a single sum or otherwise, under a contract in full discharge of the obligation under the contract which is in the nature of a refund of the consideration paid for the contract, and

"(ii) any amount received under a contract on its complete surrender, redemption, or maturity.

In the case of any amount to which the preceding sentence applies, the rule of paragraph (2)(A) shall not apply.

"(6) INVESTMENT IN THE CONTRACT.—For purposes of this subsection, the investment in the contract as of any date is—

"(A) the aggregate amount of premiums or other consideration paid for the contract before such date, minus

"(B) the aggregate amount received under the contract before such date, to the extent that such amount was excludable from gross income under this subtitle or prior income tax laws."

(b) 5-PERCENT PENALTY FOR CERTAIN PREMATURE DISTRIBUTIONS.—

(1) IN GENERAL.—Section 72 (relating to annuities; certain proceeds of endowment and life insurance contracts) is amended by redesignating subsection (q) as subsection (r) and by adding after subsection (p) the following new subsection:

"(q) 5-PERCENT PENALTY FOR PREMATURE DISTRIBUTIONS FROM ANNUITY CONTRACTS.—

"(1) IMPOSITION OF PENALTY.—

"(A) IN GENERAL.—If any taxpayer receives any amount under an annuity contract, the taxpayer's tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 5 percent of the portion of such amount includible in gross income which is properly allocable to any investment in the annuity contract made during the 10-year period ending on the date such amount was received by the taxpayer.

"(B) ALLOCATION ON FIRST-IN, FIRST-OUT BASIS.—For purposes of subparagraph (A), the amount includible in gross income shall be allocated to the earliest investment in the contract with respect to which amounts have not been previously fully allocated under this paragraph.

"(2) SUBSECTION NOT TO APPLY TO CERTAIN DISTRIBUTIONS.—This subsection shall not apply to any distribution—

"(A) made on or after the date on which the taxpayer attains age 59½,

"(B) made to a beneficiary (or to the estate of an annuitant) on or after the death of an annuitant,

"(C) attributable to the taxpayer's becoming disabled within the meaning of subsection (m)(7),

"(D) which is one of a series of substantially equal periodic payments made for the life of a taxpayer or over a period extending for at least 60 months after the annuity starting date,

"(E) from a plan, contract, account, trust, or annuity described in subsection (e)(5)(D), or

"(F) allocable to investment in the contract before August 14, 1982."

(2) CONFORMING AMENDMENTS.—

(A) Each of the following provisions are amended by inserting "section 72(q)(1) (relating to 5-percent tax on premature distributions under annuity contracts)," after "owner-employees)":

(i) Section 46(a)(4),
(ii) Section 50A(a)(3),
(iii) Section 53(a),

(iv) Section 901(a).

(B) Subparagraph (A) of section 1302(a)(2) is amended by inserting "or (q)(1)" after "section 72(m)(5)".

(C) Paragraph (1) of section 1304(e) is amended—

(i) by inserting "or section 72(q)(1) (relating to 5-percent tax on premature distributions under annuity contracts)" after "owner-employees)", and

(ii) by inserting "or (q)(1)" after "Section 72(m)(5)" in the heading thereof.

(c) EFFECTIVE DATES.—

(1) SUBSECTION (a).—The amendments made by subsection (a) shall take effect on August 13, 1982.

(2) SUBSECTION (b).—The amendments made by subsection (b) shall apply to distributions after December 31, 1982.

SEC. 266. FLEXIBLE PREMIUM CONTRACTS.

(a) IN GENERAL.—Section 101 (relating to exclusion from gross income for certain death benefits) is amended by adding at the end thereof the following new subsection:

"(f) PROCEEDS OF FLEXIBLE PREMIUM CONTRACTS PAYABLE BY REASON OF DEATH.—

"(1) IN GENERAL.—Any amount paid by reason of the death of the insured under a flexible premium life insurance contract shall be excluded from gross income only if—

"(A) under such contract—

"(i) the sum of the premiums paid under such contract does not at any time exceed the guideline premium limitation as of such time, and

"(ii) any amount payable by reason of the death of the insured (determined without regard to any qualified additional benefit) is not at any time less than the applicable percentage of the cash value of such contract at such time, or

"(B) by the terms of such contract, the cash value of such contract may not at any time exceed the net single premium with respect to the amount payable by reason of the death of the insured (determined without regard to any qualified additional benefit) at such time.

"(2) GUIDELINE PREMIUM LIMITATION.—For purposes of this subsection—

"(A) GUIDELINE PREMIUM LIMITATION.—The term 'guideline premium limitation' means, as of any date, the greater of—

"(i) the guideline single premium, or

"(ii) the sum of the guideline level premiums to such date.

"(B) GUIDELINE SINGLE PREMIUM.—The term 'guideline single premium' means the premium at issue with respect to future benefits under the contract (without regard to any qualified additional benefit), and with respect to any charges for qualified additional benefits, at the time of a determination under subparagraph (A) or (E) and which is based on—

"(i) the mortality and other charges guaranteed under the contract, and

"(ii) interest at the greater of an annual effective rate of 6 percent or the minimum rate or rates guaranteed upon issue of the contract.

"(C) GUIDELINE LEVEL PREMIUM.—The term 'guideline level premium' means the level annual amount, payable over the longest period permitted under the contract (but ending not less than 20 years from date of issue or not later than age 95, if earlier), computed on the same basis as the guideline single premium, except that subparagraph (B)(ii) shall be applied by substituting '4 percent' for '6 percent'.

"(D) COMPUTATIONAL RULES.—In computing the guideline single premium or guideline level premium under subparagraph (B) or (C)—

"(i) the excess of the amount payable by reason of the death of the insured (determined without regard to any qualified additional benefit) over the cash value of the contract shall be deemed to be not greater than such excess at the time the contract was issued,

"(ii) the maturity date shall be the latest maturity date permitted under the contract, but not less than 20 years after the date of issue or (if earlier) age 95, and

"(iii) the amount of any endowment benefit (or sum of endowment benefits) shall be deemed not to exceed the least amount payable by reason of the death of the insured (determined without regard to any qualified additional benefit) at any time under the contract.

"(E) ADJUSTMENTS.—The guideline single premium and guideline level premium shall be adjusted in the event of a change in the future benefits or any qualified additional benefit under the contract which was not reflected in any guideline single premiums or guideline level premium previously determined.

"(3) OTHER DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—

"(A) FLEXIBLE PREMIUM LIFE INSURANCE CONTRACT.—The terms 'flexible premium life insurance contract' and 'contract' mean a life insurance contract (including any qualified additional benefits) which provides for the payment of one or more premiums which are not fixed by the insurer as to both timing and amount. Such terms do not include that portion of any contract which is treated under State law as providing any annuity benefits other than as a settlement option.

"(B) PREMIUMS PAID.—The term 'premiums paid' means the premiums paid under the contract less any amounts (other than amounts includible in gross income) to which section 72(e) applies. If, in order to comply with the requirements of paragraph (1)(A), any portion of any premium paid during any contract year is returned by the insurance company (with interest) within 60 days after the end of a contract year—

"(i) the amount so returned (excluding interest) shall be deemed to reduce the sum of the premiums paid under the contract during such year, and

"(ii) notwithstanding the provisions of section 72(e), the amount of any interest so returned shall be includible in the gross income of the recipient.

"(C) APPLICABLE PERCENTAGE.—The term 'applicable percentage' means—

"(i) 140 percent in the case of an insured with an attained age at the beginning of the contract year of 40 or less, and

"(ii) in the case of an insured with an attained age of more than 40 as of the beginning of the contract year, 140 percent reduced (but not below 105 percent) by one percent for each year in excess of 40.

"(D) CASH VALUE.—The cash value of any contract shall be determined without regard to any deduction for any surrender charge or policy loan.

"(E) QUALIFIED ADDITIONAL BENEFITS.—The term 'qualified additional benefits' means any—

"(i) guaranteed insurability,

"(ii) accidental death benefit,

"(iii) family term coverage, or

"(iv) waiver of premium.

"(F) PREMIUM PAYMENTS NOT DISQUALIFYING CONTRACT.—The payment of a premium which would result in the sum of the premiums paid exceeding the guideline premium limitation shall be disregarded for purposes of paragraph (1)(A)(i) if the amount of such premium does not exceed the amount necessary to prevent the termination of the contract without cash value on or before the end of the contract year.

"(G) NET SINGLE PREMIUM.—In computing the net single premium under paragraph (1)(B)—

"(i) the mortality basis shall be that guaranteed under the contract (determined by reference to the most recent mortality table allowed under all State laws on the date of issuance),

"(ii) interest shall be based on the greater of—

"(I) an annual effective rate of 4 percent (3 percent for contracts issued before July 1, 1983), or

"(II) the minimum rate or rates guaranteed upon issue of the contract, and

"(iii) the computational rules of paragraph (2)(D) shall apply, except that the maturity date referred to in clause (ii) thereof shall not be earlier than age 95.

"(H) CORRECTION OF ERRORS.—If the taxpayer establishes to the satisfaction of the Secretary that—

"(i) the requirements described in paragraph (1) for any contract year was not satisfied due to reasonable error, and

"(ii) reasonable steps are being taken to remedy the error,

the Secretary may waive the failure to satisfy such requirements."

"(I) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subsection."

(b) CONFORMING AMENDMENT.—Paragraph (1) of section 101(a) (relating to proceeds of life insurance contracts payable by reason of death) is amended by striking out "and in subsection (d)" and inserting in lieu thereof ", subsection (d), and subsection (f)".

(c) EFFECTIVE DATES.—

(1) IN GENERAL.—The amendments made by this section shall apply to contracts entered into before January 1, 1984.

(2) SPECIAL RULE FOR CONTRACTS ENTERED INTO BEFORE JANUARY 1, 1983.—Any contract entered into before January 1, 1983, which meets the requirements of section 101(f) of the Internal Revenue Code of 1954 on the date which is 1 year after the date of the enactment of this Act shall be treated as meeting the requirements of such section for any period before the date on which such contract meets such requirements. Any death benefits paid under a flexible premium life insurance contract (within the meaning of section 101(f)(3)(A) of such Code) before the date which is 1 year after such date of enactment shall be excluded from gross income.

(3) SPECIAL RULE FOR CERTAIN CONTRACTS.—Any contract entered into before January 1, 1983, shall be treated as meeting the requirements of subparagraph (A) of section 101(f)(1) of such Code if such contract would meet such requirements if section 103(f)(2)(C) of such Code were applied by substituting "3 percent" for "4 percent".

SEC. 267. REDUCTION IN APPROXIMATE REVALUATION METHOD OF COMPUTING RESERVES.

(a) REDUCTION FROM $21 PER $1,000 TO $19 PER $1,000 IN DETERMINING APPROXIMATE REVALUATION OF CERTAIN RESERVES COMPUTED ON PRELIMINARY TERM BASIS.—

(1) IN GENERAL.—Subparagraph (A) of section 818(c)(2) (relating to approximate revaluation of reserves computed on preliminary term basis) is amended—

(A) by striking out "$21" and inserting in lieu thereof "$19", and

(B) by striking out "2.1 percent" and inserting in lieu thereof "1.9 percent".

(2) TAXPAYER ALLOWED TO ELECT OUT OF APPROXIMATE REVALUATION.—The last sentence of section 818(c) (relating to life insurance reserves computed on preliminary term basis) is amended—

(A) by inserting "or in effect for a taxable year beginning in 1981" after "1958" the first place it appears, and

(B) by inserting "or 1981, whichever is applicable" after "1958" the second place it appears.

(b) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1981, but only with respect to reserves established under contracts entered into after March 31, 1982.

PART IV—UNDERPAYMENTS OF ESTIMATED TAX FOR 1982

SEC. 268. UNDERPAYMENTS OF ESTIMATED TAX FOR 1982.

No addition to the tax shall be made under section 6655 of the Internal Revenue Code of 1954 (relating to failure by corporation to pay estimated income tax) for any period before December 15, 1982, with respect to any underpayment of estimated tax by a taxpayer with respect to any tax imposed by section 802(a), to the extent that such underpayment was created or increased by any provisions of this subtitle.

Subtitle E—Employment Taxes

PART I—IN GENERAL

SEC. 269. TREATMENT OF REAL ESTATE AGENTS AND DIRECT SELLERS.

(a) GENERAL RULE.—Chapter 25 of the Internal Revenue Code of 1954 is amended by adding at the end thereof the following new section:

"SEC. 3508. TREATMENT OF REAL ESTATE AGENTS AND DIRECT SELLERS.

"(a) GENERAL RULE.—For purposes of this title, in the case of services performed as a qualified real estate agent or as a direct seller—

"(1) the individual performing such services shall not be treated as an employee, and

"(2) the person for whom such services are performed shall not be treated as an employer.

"(b) DEFINITIONS.—For purposes of this section—

"(1) QUALIFIED REAL ESTATE AGENT.—The term 'qualified real estate agent' means any individual who is a sales person if—

"(A) such individual is a licensed real estate agent,

"(B) substantially all of the remuneration (whether or not paid in cash) for the services performed by such individual as a real estate agent is directly related to sales or other output (including the performance of services) rather than to the number of hours worked, and

"(C) the services performed by the individual are performed pursuant to a written contract between such individual and the person for whom the services are performed and such contract provides that the individual will not be treated as an employee with respect to such services for Federal tax purposes.

"(2) DIRECT SELLER.—The term 'direct seller' means any person if—

"(A) such person—

"(i) is engaged in the trade or business of selling (or soliciting the sale of) consumer products to any buyer on a buy-sell basis, a deposit-commission basis, or any similar basis which the Secretary prescribes by regulations, for resale (by the buyer or any other person) in

the home or otherwise than in a permanent retail establishment, or

"(ii) is engaged in the trade or business of selling (or soliciting the sale of) consumer products in the home or otherwise than in a permanent retail establishment,

"(B) substantially all the remuneration (whether or not paid in cash) for the performance of the services described in subparagraph (A) is directly related to sales or other output (including the performance of services) rather than to the number of hours worked, and

"(C) the services performed by the person are performed pursuant to a written contract between such person and the person for whom the services are performed and such contract provides that the person will not be treated as an employee with respect to such services for Federal tax purposes.

"(3) COORDINATION WITH RETIREMENT PLANS FOR SELF-EMPLOYED.—This section shall not apply for purposes of subtitle A to the extent that the individual is treated as an employee under section 401(c)(1) (relating to self-employed individuals)."

(b) AMENDMENT OF SOCIAL SECURITY ACT.—Section 210 of the Social Security Act is amended by adding at the end thereof the following new subsection:

"Treatment of Real Estate Agents and Direct Sellers

"(p) Notwithstanding any other provision of this title, the rules of section 3508 of the Internal Revenue Code of 1954 shall apply for purposes of this title."

(c) INDEFINITE EXTENSION OF PROVISIONS RELATING TO EMPLOYMENT STATUS FOR EMPLOYMENT TAXES.—

(1) TERMINATION OF CERTAIN EMPLOYMENT TAX LIABILITY.—

(A) Subparagraph (A) of section 530(a)(1) of the Revenue Act of 1978 (relating to termination of certain employment tax liability for periods before July 1, 1982) is amended by striking out "ending before July 1, 1982".

(B) Paragraph (3) of section 530(a) of such Act is amended by striking out "and before July 1, 1982,".

(C) The subsection heading of subsection (a) of section 530 of such Act is amended by striking out "FOR PERIODS BEFORE JULY 1, 1982".

(2) PROHIBITION AGAINST REGULATIONS AND RULINGS ON EMPLOYMENT STATUS.—Subsection (b) of section 530 of such Act is amended—

(A) by striking out "July 1, 1982 (or, if earlier,", and

(B) by striking out "taxes)" and inserting in lieu thereof "taxes".

(3) CERTAIN REGULATIONS, ETC., PERMITTED.—Nothing in section 530 of the Revenue Act of 1978 shall be construed to prohibit the implementation of the amendments made by this section.

(d) CLERICAL AMENDMENT.—The table of sections for chapter 25 of such Code is amended by adding at the end thereof the following new item:

"Sec. 3508. Treatment of real estate agents and direct sellers."

(e) EFFECTIVE DATES.—

(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section shall apply to services performed after December 31, 1982.

(2) SUBSECTION (C).—The amendments made by subsection (c) shall take effect on July 1, 1982.

SEC. 270. SIMPLIFIED PROCEDURE FOR DETERMINING AMOUNT OF EMPLOYMENT TAXES.

(a) IN GENERAL.—Chapter 25 (relating to general provisions relating to employment taxes), as amended by section 271, is amended by adding at the end thereof the following new section:

"SEC. 3509. DETERMINATION OF EMPLOYER'S LIABILITY FOR CERTAIN EMPLOYMENT TAXES.

"(a) IN GENERAL.—If any employer fails to deduct and withhold any tax under chapter 24 or subchapter A of chapter 21 with respect to any employee by reason of treating such employee as not being an employee for purposes of such chapter or subchapter, the amount of the employer's liability for—

"(1) WITHHOLDING TAXES.—Tax under chapter 24 for such year with respect to such employee shall be determined as if the amount required to be deducted and withheld were equal to 1.5 percent of the wages (as defined in section 3401) paid to such employee.

"(2) EMPLOYEE SOCIAL SECURITY TAX.—Taxes under subchapter A of chapter 21 with respect to such employee shall be determined as if the taxes imposed under such subchapter were 20 percent of the amount imposed under such subchapter without regard to this subparagraph.

"(b) EMPLOYER'S LIABILITY INCREASED WHERE EMPLOYER DISREGARDS REPORTING REQUIREMENTS.—

"(1) IN GENERAL.—In the case of an employer who fails to meet the applicable requirements of section 6041(a), 6041A, or 6051 with respect to any employee, unless such failure is due to reasonable cause and not willful neglect, subsection (a) shall be applied with respect to such employee—

"(A) by substituting '3 percent' for '1.5 percent' in paragraph (1); and

"(B) by substituting '40 percent' for '20 percent' in paragraph (2).

"(2) APPLICABLE REQUIREMENTS.—For purposes of paragraph (1), the term 'applicable requirements' means the requirements described in paragraph (1) which would be applicable consistent with the employer's treatment of the employee as not being an employee for purposes of chapter 24 or subchapter A of chapter 21.

"(c) SECTION NOT TO APPLY IN CASES OF INTENTIONAL DISREGARD.—This section shall not apply to determination of the employer's liability for tax under chapter 24 or subchapter A of chapter 21 if such liability is due to the employer's intentional disregard of the requirement to deduct and withhold such tax.

"(d) SPECIAL RULES.—For purposes of this section—

"(1) DETERMINATION OF LIABILITY.—If the amount of any liability for tax is determined under this section—

"(A) the employee's liability for tax shall not be affected by the assessment or collection of the tax so determined,

"(B) the employer shall not be entitled to recover from the employee any tax so determined, and

"(C) sections 3402(d) and section 6521 shall not apply.

"(2) SECTION NOT TO APPLY WHERE EMPLOYER DEDUCTS WAGE BUT NOT SOCIAL SECURITY TAXES.—This section shall not apply to any employer with respect to any wages if—

"(A) the employer deducted and withheld any amount of the tax imposed by chapter 24 on such wages, but

"(B) failed to deduct and withhold the amount of the tax imposed by subchapter A of chapter 21 with respect to such wages.

"(3) SECTION NOT TO APPLY TO CERTAIN STATUTORY EMPLOYEES.—This section shall not apply to any tax under subchapter A of chapter 21 with respect to an individual described in subsection (d)(3) of section 3121 (without regard to whether such individual is described in paragraph (1) or (2) of such subsection).".

(b) CONFORMING AMENDMENT.—The table of sections for chapter 25 is amended by adding at the end thereof the following new item:

"Sec. 3509. Determination of employer's liability for certain employment taxes.".

(c) EFFECTIVE DATE.—The amendment made by this section shall take effect on the date of the enactment of this Act, except that such amendments shall not apply to any assessment made before January 1, 1983.

PART II—FEDERAL UNEMPLOYMENT TAX

Subpart A—Increase in Federal Unemployment Tax

SEC. 271. INCREASE IN FEDERAL UNEMPLOYMENT TAX WAGE BASE AND RATE.

(a) INCREASE IN WAGE BASE.—Paragraph (1) of section 3306(b) (defining wages) is amended by striking out "$6,000" each place it appears and inserting in lieu thereof "$7,000".

(b) INCREASE IN RATE.—

(1) IN GENERAL.—Paragraph (1) of section 3301 (relating to rate of unemployment tax) is amended by striking out "3.4 percent" and inserting in lieu thereof "3.5 percent".

(2) TECHNICAL AMENDMENTS.—

(A) Subparagraph (C) of section 901(c)(3) of the Social Security Act is amended to read as follows:

"(C) Each estimate of net receipts under this paragraph shall be based upon (i) a tax rate of 0.5 percent in the case of any calendar year for which the rate of tax under section 3301 of the Federal Unemployment Tax Act is 3.2 percent, and (ii) a tax rate of 0.8 percent in the case of any calendar year for which the rate of tax under such section is 3.5 percent."

(B) Paragraph (1) of section 905(b) of such Act is amended by amending the last sentence to read as follows: "In the

case of any month after March 1983 and before April 1 of the first calendar year to which paragraph (2) of section 3301 of the Federal Unemployment Tax Act applies, the first sentence of this paragraph shall be applied by substituting '40 percent' for 'one-tenth'."

(C) Subsection (b) of section 6157 is amended by striking out "0.7 percent" and inserting in lieu thereof "0.8 percent".

(c) INCREASE IN RATE FOR 1985 AND THEREAFTER.—

(1) IN GENERAL.—Section 3301 (as amended by subsection (b)) is amended—

(A) by striking out "3.5 percent" and inserting in lieu thereof "6.2 percent", and

(B) by striking out "3.2 percent" and inserting in lieu thereof "6.0 percent".

(2) INCREASE IN AMOUNT OF STATE CREDIT.—

(A) Subsection (b) of section 3302 (relating to additional credit) is amended by striking out "2.7%" and inserting in lieu thereof "5.4%".

(B) Paragraph (1) of section 3302(d) (relating to rate of tax deemed to be 3 percent) is amended by striking out "3 percent" each place it appears and inserting in lieu thereof "6 percent".

(3) TECHNICAL AMENDMENTS.—

(A) Paragraph (2) of section 3302(c) is amended by striking out "10 percent" each place it appears in subparagraph (A) and inserting in lieu thereof "5 percent".

(B) Paragraph (3) of section 3302(c) is amended by striking out "15 percent" and inserting in lieu thereof "7½ percent".

(C) Subsection (b) of section 6157 is amended by striking out "0.5 percent" each place it appears and inserting in lieu thereof "0.6 percent".

(D) Subparagraph (C) of section 901(c)(3) of the Social Security Act (as amended by subsection (b)) is amended—

(i) by striking out "0.5 percent" and inserting in lieu thereof "0.6 percent";

(ii) by striking out "3.2 percent" and inserting in lieu thereof "6.0 percent"; and

(iii) by striking out "3.5 percent" and inserting in lieu thereof "6.2 percent".

(b) EFFECTIVE DATES.—

(1) SUBSECTIONS (a) AND (b).—The amendments made by subsections (a) and (b) shall apply to remuneration paid after December 31, 1982.

(2) SUBSECTION (c).—The amendments made by subsection (c) shall apply to remuneration paid after December 31, 1984.

(3) TRANSITIONAL RULE FOR CERTAIN EMPLOYEES.—

(A) IN GENERAL.—Notwithstanding section 3303 of the Internal Revenue Code of 1954, in the case of taxable years beginning after December 31, 1984, and before January 1, 1989, a taxpayer shall be allowed the additional credit under section 3302(b) of such Code with respect to any employee covered by a qualified specific industry provision if

the requirements of subparagraph (B) are met with respect to such employee.

(B) Requirements.—The requirements of this subparagraph are met for any taxable year with respect to any employee covered by a specific industry provision if the amount of contributions required to be paid for the taxable year to the unemployment fund of the State with respect to such employee are not less than the product of the required rate multiplied by the wages paid by the employer during the taxable year.

(C) Required rate.—For purposes of subparagraph (B), the required rate for any taxable year is the sum of—

(i) the rate at which contributions were required to be made under the specific industry provision as in effect on August 10, 1982, and

(ii) the applicable percentage of the excess of 5.4 percent over the rate described in clause (i).

(D) Applicable percentage.—For purposes of subparagraph (C), the term "applicable percentage" means—

(i) 20 percent in the case of taxable year 1985,

(ii) 40 percent in the case of taxable year 1986,

(iii) 60 percent in the case of taxable year 1987, and

(iv) 80 percent in the case of taxable year 1988.

(E) Qualified specific industry provision.—For purposes of this paragraph, the term, "qualified specific industry provision" means a provision contained in a State unemployment compensation law (as in effect on August 10, 1982)—

(i) which applies to employees in a specific industry or to an otherwise defined type of employees, and

(ii) under which employers may elect to make contributions at a specified rate (without experience rating) which exceeds 2.7 percent.

Subpart B—Other Financing Provisions

SEC. 272. CREDIT REDUCTION NOT TO APPLY WHEN STATE MAKES CERTAIN REPAYMENTS.

(a) General Rule.—Section 3302 (relating to credits against unemployment tax) is amended by adding at the end thereof the following new subsection:

"(g) Credit Reduction Not To Apply When State Makes Certain Repayments.—

"(1) In general.—In the case of any State which meets requirements of paragraph (2) with respect to any taxable year, subsection (c)(2) shall not apply to such taxable year; except that such taxable year (and January 1 of such taxble year) shall (except as provided in subsection (f)(3)) be taken into account for purposes of applying subsection (c)(2) to succeeding taxable years.

"(2) Requirements.—The requirements of this paragraph are met by any State with respect to any taxable year if the Secretary of Labor determines that—

"(A) the repayments during the 1-year period ending on November 9 of such taxable year made by such State of advances under title XII of the Social Security Act are not less than the sum of—

"(i) the potential additional taxes for such taxable year, and

(ii) any advances made to such State during such 1-year period under such title XII,

"(B) there will be sufficient amounts in the State unemployment fund to pay all compensation during the 3-month period beginning on November 1 of such taxable year without receiving any advance under title XII of the Social Security Act, and

"(C) there is a net increase in the solvency of the State unemployment compensation system for the taxable year attributable to changes made in the State law after the date on which the first advance taken into account in determining the amount of the potential additional taxes was made (or, if later, after the date of the enactment of this subsection) and such net increase equals or exceeds the potential additional taxes for such taxable year.

"(3) Definitions.—For purposes of paragraph (2)—

"(A) Potential additional taxes.—The term 'potential additional taxes' means, with respect to any State for any taxable year, the aggregate amount of the additional tax which would be payable under this chapter for such taxable year by all taxpayers subject to the unemployment compensation law of such State for such taxable year if paragraph (2) of subsection (c) had applied to such taxable year and any preceding taxable year without regard to this subsection but with regard to subsection (f).

"(B) Treatment of certain reductions.—Any reduction in the State's balance under section 901(d)(1) of the Social Security Act shall not be treated as a repayment made by such State.

"(4) Reports.—The Secretary of Labor may require a State to furnish such information at such time and in such manner as may be necessary for purposes of paragraph (2)."

(b) Effective Date.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1982.

SEC. 273. LIMITATION ON FIFTH YEAR CREDIT REDUCTION.

(a) General Rule.—Paragraph (2) of section 3302(c) (relating to limit on total credits) is amended by adding at the end thereof the following new sentence: "Subparagraph (C) shall not apply with respect to any taxable year to which it would otherwise apply (but subparagraph (B) shall apply to such taxable year) if the Secretary of Labor determines (on or before November 10 of such taxable year) that the State meets the requirements of subsection (f)(2)(B) for such taxable year."

(b) Effective Date.—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1982.

SEC. 274. DEFERRAL OF INTEREST IN CASE OF CERTAIN STATES WITH HIGH UNEMPLOYMENT RATES.

(a) GENERAL RULE.—Paragraph (3) of section 1202(b) of the Social Security Act is amended by adding at the end thereof the following new subparagraph:

"(C)(i) In the case of any State which meets the requirements of clause (ii) for any calendar year, any interest otherwise required to be paid under this subsection during such calendar year shall be paid as follows—

"(I) 25 percent of the amount otherwise required to be paid on or before any day during such calendar year shall be paid on or before such day; and

"(II) 25 percent of the amount otherwise required to be paid on or before such day shall be paid on or before the corresponding day in each of the 3 succeeding calendar years.

Any interest the time for payment of which is deferred under this subparagraph shall bear interest in the same manner as if it were an advance made on the day on which it would have been required to be paid but for this subparagraph.

"(ii) A State meets the requirements of this clause for any calendar year if the rate of insured unemployment (as determined for purposes of section 203 of the Federal-State Extended Unemployment Compensation Act of 1970) under the State law of the period consisting of the first 6 months of the preceding calendar year equaled or exceeded 7.5 percent."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to interest required to be paid after December 31, 1982.

SEC. 275. REQUIRED REPAYMENTS FROM EXTENDED UNEMPLOYMENT COMPENSATION ACCOUNT.

Subsection (d) of section 905 of the Social Security Act is amended by inserting after the second sentence the following new sentence: "Repayments under the preceding sentence shall be made whenever the Secretary of the Treasury (after consultation with the Secretary of Labor) determines that the amount then in the account exceeds the amount necessary to meet the anticipated payments from the account during the next 3 months."

SEC. 276. TREATMENT OF CERTAIN SERVICES PERFORMED BY STUDENTS.

(a) STUDENT INTERNS.—

(1) IN GENERAL.—Subparagraph (C) of section 3306(c)(10) (defining employment) is amended by striking out "under the age of 22".

(2) EFFECTIVE DATE.—The amendment made by paragraph (1) shall apply with respect to services performed after the date of the enactment of this Act.

(b) FULL TIME STUDENTS EMPLOYED BY SUMMER CAMPS.—

(1) SERVICE BY FULL TIME STUDENTS.—Subsection (c) of section 3306 (defining employment) is amended—

(A) by striking out "or" at the end of paragraph (18),

(B) by striking out the period at the end of paragraph (19) and inserting in lieu thereof "; or", and

(C) by adding at the end thereof the following new paragraph:

"(20) service performed by a full time student (as defined in subsection (q)) in the employ of an organized camp—

"(A) if such camp—

"(i) did not operate for more than 7 months in the calendar year and did not operate for more than 7 months in the preceding calendar year, or

"(ii) had average gross receipts for any 6 months in the preceding calendar year which were not more than 33⅓ percent of its average gross receipts for the other 6 months in the preceding calendar year; and

"(B) if such full time student performed services in the employ of such camp for less than 13 calendar weeks in such calendar year."

(2) FULL TIME STUDENT DEFINED.—Section 3306 is amended by adding at the end thereof the following new subsection:

"(q) FULL TIME STUDENT.—For purposes of subsection (c)(20), an individual shall be treated as a full time student for any period—

"(1) during which the individual is enrolled as a full time student at an educational institution, or

"(2) which is between academic years or terms if—

"(A) the individual was enrolled as a full time student at an educational institution for the immediately preceding academic year or term, and

"(B) there is a reasonable assurance that the individual will be so enrolled for the immediately succeeding academic year or term after the period described in subparagraph (A)."

(3) EFFECTIVE DATE.—The amendments made by this subsection shall apply to remuneration paid after December 31, 1982, and before January 1, 1984.

SEC. 277. TREATMENT OF CERTAIN ALIEN FARM WORKERS.

Subparagraph (B) of section 3306(c)(1) (defining employment) is amended by striking out "January 1, 1982" and inserting in lieu thereof "January 1, 1984".

PART III—MEDICARE COVERAGE

SEC. 278. MEDICARE COVERAGE OF, AND APPLICATION OF HOSPITAL INSURANCE TAX TO, FEDERAL EMPLOYMENT.

(a) APPLICATION OF HOSPITAL INSURANCE TAX TO FEDERAL EMPLOYMENT.—

(1) IN GENERAL.—Section 3121 (relating to definitions for purposes of the Federal Insurance Contributions Act) is amended by adding at the end thereof the following new subsection:

"(u) APPLICATION OF HOSPITAL INSURANCE TAX TO FEDERAL EMPLOYMENT.—

"(1) IN GENERAL.—For purposes of the taxes imposed by sections 3101(b) and 3111(b)—

"(A) paragraph (6) of subsection (b) shall be applied without regard to subparagraphs (A), (B), and (C)(i), (ii), and (vi) thereof, and

"(B) paragraph (5) of subsection (b) (and the provisions of law referred to therein) shall not apply.

"(2) Medicare qualified federal employment.—For purposes of this chapter, the term 'medicare qualified Federal employment' means service which—

"(A) is employment (as defined in subsection (b)) with the application of paragraph (1), but

"(B) would not be employment (as so defined) without the application of paragraph (1)."

(2) Conforming amendment to self-employment tax.—Section 1402(b) (relating to self-employment income) is amended in the second sentence by striking out "and" before "(B)" and by inserting before the period the following: ", and (C) includes, but only with respect to the tax imposed by section 1401(b), remuneration paid for medicare qualified Federal employment (as defined in section 3121(u)(2)) which is subject to the taxes imposed by sections 3101(b) and 3111(b)".

(3) Conforming amendment to federal service.—Section 3122 (relating to federal service) is amended in the first sentence by inserting "including service which is medicare qualified Federal employment (as defined in section 3121(u)(2))," after "wholly owned by the United States,".

(b) Entitlement to Hospital Insurance Benefits.—

(1) Definition of medicare qualified federal employment.—Section 210 of the Social Security Act is amended by adding at the end thereof the following new subsection:

"Medicare Qualified Federal Employment

"(p) For purposes of sections 226 and 226A, the term 'medicare qualified Federal employment' means any service which would constitute 'employment' as defined in subsection (a) of this section but for the application of the provisions of—

"(1) subparagraph (A), (B), or (C)(i), (ii), or (vi) of subsection (a)(6), or

"(2) subsection (a)(5).".

(2) Entitlement to hospital insurance benefits.—

(A) For individuals age 65 or older.—Section 226(a)(2) of the the Social Security Act is amended—

(i) by inserting "(A)" after "(2)";

(ii) by striking out "or is a qualified railroad retirement beneficiary," at the end of subparagraph (A); and

(iii) by inserting after subparagraph (A) the following new subparagraphs:

"(B) is a qualified railroad retirement beneficiary, or

"(C)(i) would meet the requirements of subparagraph (A) upon filing application for the monthly insurance benefits involved if medicare qualified Federal employment (as defined in section 210(p)) were treated as employment (as defined in section 210(a)) for purposes of this title, and (ii) files an application, in conformity with regulations of the Secretary, for hospital insurance benefits under part A of title XVIII,".

(B) Entitlement for disabled individuals.—

(i) In general.—Section 226(b)(2) of the Social Security Act is amended by striking out "(B)" and all that

follows through "1974," and adding at the end the following:

"(B) is, and has been for not less than 24 months, a disabled qualified railroad retirement beneficiary, within the meaning of section 7(d) of the Railroad Retirement Act of 1974, or

"(C)(i) has filed an application, in conformity with regulations of the Secretary, for hospital insurance benefits under part A of title XVIII pursuant to this subparagraph, and

"(ii) would meet the requirements of subparagraph (A) (as determined under the disability criteria, including reviews, applied under this title), including the requirement that he have been entitled to the specified benefits for 24 months, if—

"(I) medicare qualified Federal employment (as defined in section 210(p)) were treated as employment (as defined in section 210(a)) for purposes of this title, and

"(II) the filing of the application under clause (i) of this subparagraph were deemed to be the filing of an application for the disability-related benefits referred to in clause (i), (ii), or (iii) of subparagraph (A),".

(ii) CLARIFICATION OF PERIOD OF ENTITLEMENT.—Section 226(b) of such Act is further amended by adding after the first sentence the following new sentence: "In applying the previous sentence in the case of an an individual described in paragraph (2)(C), the 'twenty-fifth month of his entitlement' refers to the first month after the twenty-fourth month of entitlement to specified benefits referred to in paragraph (2)(C) and 'notice of termination of such entitlement' refers to a notice that the individual would no longer be determined to be entitled to such specified benefits under the conditions described in that paragraph.".

(C) ENTITLEMENT FOR INDIVIDUALS WITH END-STAGE RENAL DISEASE.—Paragraph (1) of section 226A(a) of the Social Security Act is amended to read as follows:

"(1)(A) is fully or currently insured (as such terms are defined in section 214), or would be fully or currently insured if (i) his service as an employee (as defined in the Railroad Retirement Act of 1974) after December 31, 1936, were included within the meaning of the term 'employment' for purposes of this title, and (ii) his medicare qualified Federal employment (as defined in section 210(p)) were included within the meaning of the term 'employment' for purposes of this title;

"(B)(i) is entitled to monthly insurance benefits under this title, (ii) is entitled to an annuity under the Railroad Retirement Act of 1974, or (iii) would be entitled to a monthly insurance benefit under this title if medicare qualified Federal employment (as defined in 210(p)) after December 31, 1982, were included within the meaning of the term 'employment' for purposes of this title; or

"(C) is the spouse or dependent child (as defined in regulations) of an individual described in subparagraph (A) or (B);".

(3) CONFORMING AMENDMENT.—Section 1811 of the Social Security Act is amended—

(A) by inserting "(or would be eligible for such benefits if certain Federal employment were covered employment under such title)" after "title II of this Act" in clause (1), and

(B) by inserting "(or would have been so entitled to such benefits if certain Federal employment were covered employment under such title)" after "title II of this Act" in clause (2).

(4) NOTICE TO INDIVIDUALS WHO ARE PROSPECTIVE MEDICARE BENEFICIARIES BASED ON FEDERAL EMPLOYMENT.—Section 226 of such Act is amended by redesignating subsection (g) as subsection (h) and by inerting after subsection (f) the following new subsection:

"(g) The Secretary and Director of the Office of Personnel Management shall jointly prescribe and carry out procedures designed to assure that all individuals who perform medicare qualified Federal employment are fully informed with respect to (1) their eligibility or potential eligibility for hospital insurance benefits (based on such employment) under part A of title XVIII, (2) the requirements for and conditions of such eligibility, and (3) the necessity of timely application as a condition of entitlement under subsection (b)(2)(C), giving particular attention to individuals who apply for an annuity under chapter 83 of title 5, United States Code, or under another similar Federal retirement program, and whose eligibility for such an annuity is or would be based on a disability.".

(c) EFFECTIVE DATES.—

(1) HOSPITAL INSURANCE TAXES.—The amendments made by subsection (a) shall apply to remuneration paid after December 31, 1982.

(2) MEDICARE COVERAGE.—

(A) IN GENERAL.—The amendments made by subsection (b) are effective on and after January 1, 1983, and the amendments made by paragraph (3) of that subsection apply to remuneration (for medicare qualified Federal employment) paid after December 31, 1982.

(B) TREATMENT OF CURRENT DISABILITIES.—For purposes of establishing entitlement to hospital insurance benefits under part A of title XVIII of the Social Security Act pursuant to the amendments made by subsection (b) or the provisions of subsection (d), no individual may be considered to be under a disability for any period before January 1, 1983.

(d) TRANSITIONAL PROVISIONS.—

(1) IN GENERAL.—For purposes of sections 226, 226A, and 1811 of the Social Security Act, in the case of any individual—

(A) who performs service both during January 1983, and before January 1, 1983, which constitutes medicare qualified Federal employment (as defined in section 210(p) of such Act) and

(B) who would be entitled, under section 226(a)(2)(C), 226(b)(2)(C), 226A(a)(1)(A)(ii), or 226A(a)(1)(B)(iii) of such Act, to hospital insurance benefits under part A ot title XVIII of such Act but for the failure to include medicare qualified Federal employment (as so defined) within the

meaning of the term "employment" for purposes of title II of such Act for remuneration paid before January 1, 1983, the individual's medicare qualified Federal employment (as so defined) performed before January 1, 1983, for which remuneration was paid before such date, shall be considered to be "employment" (as so defined), but only for the purpose of providing such entitlement.

(2) ELIGIBILITY OF OTHER PERSONS.—Any individual who is entitled to hospital insurance benefits under part A of title XVIII of the Social Security Act by reason of the application of paragraph (1) of this subsection, shall be deemed to be entitled to an old-age benefit under section 202 of such Act, or a disability benefit under section 223 of such Act, for purposes of determining eligibility for such hospital insurance benefits for any other person. In applying this paragraph, any such other person who would be entitled to a monthly benefit under section 202 of such Act if such individual (to whom paragraph (1) applies) were entitled to such old-age or disability benefit, shall be deemed to be entitled to such monthly benefit, but only for purposes of determining such person's eligibility for hospital insurance benefits.

(3) APPROPRIATIONS.—There are authorized to be appropriated to the Federal Hospital Insurance Trust Fund from time to time such sums as the Secretary of Health and Human Services deems necessary for any fiscal year, on account of—

(A) payments made or to be made during such fiscal year from such Trust Fund with respect to individuals who are entitled to benefits under title XVIII of the Social Security Act solely by reason of paragraph (1) or (2) of this subsection,

(B) the additional adminstrative expenses resulting or expected to result therefrom, and

(C) any loss in interest to such Trust Fund resulting from the payment of those amounts,

in order to place such Trust Fund in the same position at the end of such fiscal year as it would have been in if this subsection had not been enacted.

Subtitle F—Excise Taxes

PART I—AIRPORT AND AIRWAY

SEC. 279. TAX ON FUEL USED IN NONCOMMERCIAL AVIATION.

(a) IMPOSITION OF TAX.—

(1) GASOLINE FUELS.—Paragraph (3) of subsection 4041(c) (relating to rate of tax) is amended by striking out "3 cents a gallon" and inserting in lieu thereof "8 cents a gallon (10½ cents a gallon in the case of any gasoline with respect to which a tax is imposed under section 4081 at the rate set forth in subsection (b) thereof)".

(2) NONGASOLINE FUELS.—Paragraph (1) of subsection 4041(c) (relating to tax on fuel used in non-commercial aviation) is

amended by striking out "7 cents" and inserting in lieu thereof "14 cents".

(3) Termination.—Paragraph (5) of section 4041(c) is amended to read as follows:

"(5) Termination.—The taxes imposed by paragraphs (1) and (2) shall apply during the period beginning on September 1, 1982, and ending on December 31, 1987."

(b) Certain Helicopters.—

(1) Exemption.—Section 4041 (relating to tax on special fuels) is amended by adding at the end thereof the following new subsection:

"(l) Exemption For Certain Helicopter Uses.—No tax shall be imposed under this section on any liquid sold for use in, or used in, a helicopter for the purpose of—

"(1) transporting individuals, equipment, or supplies in the exploration for, or the development or removal of, hard minerals, or

"(2) the planting, cultivation, cutting or transportation of, or caring for, trees (including logging operation),

but only if the helicopter does not take off from, or land at a facility eligible for assistance under the Airport and Airway Development Act of 1970, or otherwise use services provided pursuant to the Airport and Airway System Development Act of 1982 during such use."

(2) Refund of tax.— Subsection (d) of section 6427 (relating to fuels not used for taxable purposes) is amended—

(A) by inserting "or is used in a helicopter for a purpose described in section 4041(l)," after "section 4041(h)(2)(C),"; and

(B) by inserting "or in Certain Helicopters" after "Museums" in the caption thereof.

(c) Effective Date.—The amendments made by this section shall take effect on September 1, 1982.

SEC. 280. TAX ON TRANSPORTATION BY AIR

(a) Transportation of Persons.—Section 4261 (relating to imposition of tax) is amended by striking out subsection (e) and inserting in lieu thereof the following new subsections:

"(e) Exemption for Certain Helicopter Uses.—No tax shall be imposed under subsection (a) or (b) on air transportation by helicopter for the purpose of—

"(1) transporting individuals, equipment, or supplies in the exploration for, or the development or removal of, hard minerals, or

"(2) the planting, cultivation, cutting, or transportation of, or caring for, trees (including logging operations),

but only if the helicopter does not take off from, or land at, a facility eligible for assistance under the Airport and Airway Development Act of 1970, or otherwise use services provided pursuant to the Airport and Airway System Development Act of 1982 during such use.

"(f) Termination.—The taxes imposed by this section shall apply with respect to transportation beginning after August 31, 1982, and before January 1, 1988."

(b) Transportation of Property.—Subsection (d) of section 4271 is amended to read as follows:

"(d) Termination.—The tax imposed by subsection (a) shall apply with respect to transportation beginning after August 31, 1982, and before January 1, 1988."

(c) Repeal of Certain Terminated Taxes.—

(1) In general.—Subchapter E of chapter 36 is hereby repealed.

(2) Conforming amendments.—

(A) The table of subchapters for chapter 36 is amended by striking out the item relating to subchapter E.

(B) Section 4281 (relating to small aircraft on nonestablished lines) is amended—

(i) by striking out "(as defined in section 4492(b))", and

(ii) by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, the term 'maximum certificated takeoff weight' means the maximum such weight contained in the type certificate or airworthiness certificate."

(C) Subsection (a) of section 6156 is amended by striking out "or 4491".

(D) Paragraph (2) of section 6156(e) is amended by striking out "in the case of the tax imposed by section 4481".

(E) The section heading for section 6156 is amended by striking out "AND CIVIL AIRCRAFT".

(F) The table of sections for subchapter A of chapter 62 is amended by striking out "and civil aircraft" in the item relating to section 6156.

(G) Section 6426 is hereby repealed.

(H) The table of sections for subchapter B of chapter 65 is amended by striking out the item relating to section 6426.

(d) Effective Date.—The amendments made by this section shall apply with respect to transportation beginning after August 31, 1982; except that such amendments shall not apply to any amount paid on or before such date.

SEC. 281. EXTENSION OF AIRPORT AND AIRWAY TRUST FUND.

(a) General Rule.—Subchapter A of chapter 98 (relating to Trust Fund Code) is amended by adding at the end thereof the following new section:

"SEC. 9502. AIRPORT AND AIRWAY TRUST FUND.

"(a) Creation of Trust Fund.—There is established in the Treasury of the United States a trust fund to be known as the 'Airport and Airway Trust Fund', consisting of such amounts as may be appropriated or credited to the Airport and Airway Trust Fund as provided in this section or section 9602(b).

"(b) Transfer to Airport and Airway Trust Fund of Amounts Equivalent to Certain Taxes.—There is hereby appropriated to the Airport and Airway Trust Fund—

"(1) amounts equivalent to the taxes received in the Treasury after August 31, 1982, and before January 1, 1988, under subsections (c) and (d) of section 4041 (taxes on aviation fuel) and under sections 4261 and 4271 (taxes on transportation by air);

"(2) amounts determined by the Secretary of the Treasury to be equivalent to the taxes received in the Treasury after August 31, 1982, January 1, 1988, under section 4081, with respect to gasoline used in aircraft; and

"(3) amounts determined by the Secretary of the Treasury to be equivalent to the taxes received in the Treasury after August 31, 1982, January 1, 1988 under paragraphs (2) and (3) of section 4071(a), with respect to tires and tubes of the types used on aircraft.

"(c) APPROPRIATION OF ADDITIONAL SUMS.—There are hereby authorized to be appropriated to the Airport and Airway Trust Fund such additional sums as may be required to make the expenditures referred to in subsection (d) of this section.

"(d) EXPENDITURES FROM AIRPORT AND AIRWAY TRUST FUND.—

"(1) AIRPORT AND AIRWAY PROGRAM.—Amounts in the Airport and Airway Trust Fund shall be available, as provided by appropriation Acts, for making expenditures before October 1, 1987, to meet those obligations of the United States—

"(A) incurred under title I of the Airport and Airway Development Act of 1970 or of the Airport and Airway Development Act Amendments of 1976 or of the Aviation Safety and Noise Abatement Act of 1979 (as such Acts were in effect on the date of enactment of the Fiscal Year 1981 Airport Development Authorization Act) or under the Fiscal Year 1981 Airport Development Authorization Act or the provisions of the Airport and Airway System Development Act of 1982;

"(B) heretofore or hereafter incurred under the Federal Aviation Act of 1958, as amended (49 U.S.C. 1301 et seq.), which are attributable to planning, research and development, construction, or operation and maintenance of—

"(i) air traffic control,

"(ii) air navigation,

"(iii) communications, or

"(iv) supporting services,

for the airway system; or

"(C) for those portions of the administrative expenses of the Department of Transportation which are attributable to activities described in subparagraph (A) or (B).

"(2) TRANSFERS FROM AIRPORT AND AIRWAY TRUST FUND ON ACCOUNT OF CERTAIN REFUNDS.—The Secretary of the Treasury shall pay from time to time from the Airport and Airway Trust Fund into the general fund of the Treasury amounts equivalent to the amounts paid after August 31, 1982, in respect of fuel used in aircraft, under section 6420 (relating to amounts paid in respect of gasoline used on farms), 6421 (relating to amounts paid in respect of gasoline used for certain nonhighway purposes), or 6427 (relating to fuels not used for taxable purposes).

"(3) TRANSFERS FROM THE AIRPORT AND AIRWAY TRUST FUND ON ACCOUNT OF CERTAIN SECTION 39 CREDITS.—The Secretary of the Treasury shall pay from time to time from the Airport and Airway Trust Fund into the general fund of the Treasury amounts equivalent to the credits allowed under section 39 with respect to fuel used after August 31, 1982. Such amounts shall

be transferred on the basis of estimates by the Secretary of the Treasury, and proper adjustments shall be made in amounts subsequently transferred to the extent prior estimates were in excess of or less than the credits allowed.".

(b) Repeal of Section 208 of the Airport and Airway Revenue Act of 1970.—Section 208 of the Airport and Airway Revenue Act of 1970 is hereby repealed.

(c) Conforming Amendments.—

(1) The table of sections for subchapter A of chapter 98 is amended to read as follows:

"Sec. 9501. Black Lung Disability Trust Fund.
"Sec. 9502. Airport and Airway Trust Fund.".

(2) The section heading for section 9501 (relating to establishment of Black Lung Disability Trust Fund) is amended to read as follows:

"SEC. 9501. BLACK LUNG DISABILITY TRUST FUND.".

(d) Effective Date.—

(1) In general.—The amendments made by this section shall take effect on September 1, 1982.

(2) Savings provisions.—The Airport and Airway Trust Fund established by the amendments made by this section shall be treated for all purposes of law as the continuation of the Airport and Airway Trust Fund established by section 208 of the Airport and Airway Revenue Act of 1970. Any reference in any law to the Airport and Airway Trust Fund established by such section 208 shall be deemed to include a reference to the Airport and Airway Trust Fund established by the amendments made by this section.

PART II—COMMUNICATIONS SERVICES

SEC. 284. EXTENSION OF EXCISE TAX ON COMMUNICATIONS SERVICES.

(a) In General.—Section 4251 (relating to imposition of tax on communications services) is amended by striking out subsections (a) and (b) and inserting the following new subsections:

"(a) Tax Imposed.—

"(1) In general.—There is hereby imposed on amounts paid for communications services a tax equal to the applicable percentage of amounts so paid.

"(2) Payment of tax.—The tax imposed by this section shall be paid by the person paying for such services.

"(b) Definitions.—For purposes of subsection (a)—

"(1) Communications services.—The term 'communications services' means—

"(A) local telephone service;

"(B) toll telephone service; and

"(C) teletypewriter exchange service.

"(2) Applicable percentage.—The term 'applicable percentage' means—

"With respect to amounts paid pursuant to bills first rendered—	*The percentage is—*
During 1983, 1984, or 1985	*3*
During 1986 or thereafter	*0."*

(b) Effective Date.—The amendment made by subsection (a) shall apply with respect to amounts paid for communications services pursuant to bills first rendered after December 31, 1982.

PART III—CIGARETTES

SEC. 283. INCREASE IN TAX ON CIGARETTES.

(a) Rate of Tax.—Subsection (b) of section 5701 (relating to rate of tax on cigarettes) is amended—

(1) by striking out "$4" in paragraph (1) and inserting in lieu thereof "$8; and

(2) by striking out "8.40" in paragraph (2) and inserting in lieu thereof $16.80".

(b) Floor Stocks.—

(1) Imposition of tax.—On cigarettes manufactured in or imported into the United States which are removed before January 1, 1983, and held on such date for sale by any person, there shall be imposed the following taxes:

(A) Small cigarettes.—On cigarettes, weighing not more than 3 pounds per thousand, $4 per thousand;

(B) Large cigarettes.—On cigarettes, weighing more than 3 pounds per thousand $8.40 per thousand; except that, if more than 6½ inches in length, they shall be taxable at the rate prescribed for cigarettes weighing not more than 3 pounds per thousand, counting each 2¾ inches, or fraction thereof, of the length of each as one cigarette.

(2) Liability for Tax and Method of Payment.—

(A) Liability for tax.—A person holding cigarettes on January 1, 1983, to which any tax imposed by paragraph (1) applies shall be liable for such tax.

(B) Method of payment.—The tax imposed by paragraph (1) shall be treated as a tax imposed under section 5701 and shall be due and payable on January 18, 1983 in the same manneras the tax imposed under such section is payable with respect to cigarettes removed on after January 1, 1983.

(3) Cigarette.—For purposes of this subsection, the term "cigarette" shall have the meaning given to such term by subsection (b) of section 5702 of the Internal Revenue Code of 1954.

(4) Exception for retailers.—The taxes imposed by paragraph (1) shall not apply to cigarettes in retail stocks held on January 1, 1983, at the place where intended to be sold at retail.

(c) Effective Date.—The amendment made by subsection (a) shall apply with respect to cigarettes removed after December 31, 1982 and before October 1, 1985.

PART IV—TAPS ADJUSTMENT ELIMINATED

SEC. 284. ELIMINATION OF THE TAPS ADJUSTMENT.

(a) In General.—Subsection (d) of section 4996 (relating to Alaskan oil from Sadlerochit reservior) is amended to read as follows:

"(d) Alaskan Oil From Sadlerochit Reservoir.—For purposes of this chapter—

"(1) Removal price determined on monthly basis.—The removal price of Sadlerochit oil removed during any calendar month shall be the average of the producer's removal prices for such month.

"(2) Sadlerochit oil defined.—The term 'Sadlerochit oil' means crude oil produced from the Sadlerochit reservoir in the Prudhoe Bay oilfield.".

(b) Effective Date.—The amendment made by this section shall apply with respect to oil removed after December 31, 1982.

Subtitle G—Miscellaneous

SEC. 285. TWO-YEAR EXTENSION OF EXCLUSION FROM GROSS INCOME OF NATIONAL RESEARCH SERVICE AWARDS.

Paragraph (2) of section 161(b) of the Revenue Act of 1978 relating to exclusion from gross income for national research service awards) is amended by striking out "1981" and inserting in lieu thereof "1983".

SEC. 286. SPECIAL RULES FOR CERTAIN AMATEUR SPORTS ORGANIZATIONS.

(a) Special Rules.—Section 501 is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:

"(j) Special Rules for Certain Amateur Sports Organizations.—

"(1) In general.—In the case of a qualified amateur sports organization—

"(A) the requirement of subsection (c)(3) that no part of its activities involve the provision of athletic facilities or equipment shall not apply, and

"(B) such organization shall not fail to meet the requirements of subsection (c)(3) merely because its membership is local or regional in nature.

"(2) Qualified amateur sports organization defined.—For purposes of this subsection, the term 'qualified amateur sports organization' means any organization organized and operated exclusively to foster national or international amateur sports competition if such organization is also organized and operated primarily to conduct national or international competition in sports or to support and develop amateur athletes for national or international competition in sports."

(b) Definition of Charitable Contribution.—(1) Subsection (c) of section 170 (defining charitable contribution) is amended by adding at the end of paragraph (2) the following new sentence: "Rules similar to the rules of section 501(j) shall apply for purposes of this paragraph".

(2) Subsection (a) of section 2055 (relating to transfers for public, charitable, and religious uses) is amended by adding at the end thereof the following new sentence: "Rules similar to the rules of section 501(j) shall apply for purposes of paragraph (2).".

(3) Subsection (a) of section 2522 (relating to charitable and similar gifts) is amended by adding at the end thereof the following new

sentence: "Rules similar to the rules of section 501(j) shall apply for purposes of paragraph (2).".

(c) Effective Date.—The amendments made by this section shall take effect on October 5, 1976.

SEC. 287. NEW JERSEY GENERAL REVENUE SHARING ALLOCATION.

(a) In General.—Subsection (e) of section 109 of the State and Local Fiscal Assistance Act of 1972 (31 U.S.C. 1228) (defining general tax effort factor) is amended by inserting at the end thereof the following new paragraph:

"(3) New Jersey franchise and gross receipts taxes.—

"(A) The New Jersey Franchise and Gross Receipts Taxes (N.J. Rev. Stat. 54:30A–18.1) transferred to a unit of local government within the State in the years beginning January 1 of 1980, 1981, and 1982 shall be deemed to be an adjusted tax of such units for purposes of paragraph (2)(A)(i).

"(B) The provisions of subparagraph (A) shall be given effect for quarterly payments made for quarters beginning after December 31, 1982, only if the Governor of the State of New Jersey notifies the Secretary that, prior to January 1, 1983, the State amended the New Jersey Franchise and Gross Receipts Taxes statute to provide for collection and retention of such taxes by units of local government for years beginning as of January 1, 1983.

"(C) Notwithstanding the limitation in subparagraph (B), the provisions of subparagaph (A) shall be given effect with respect to the quarterly payment to be made for the quarter beginning October 1, 1982.".

(b) Effective Date.—The amendment made by this section shall be effective after September 30, 1982.

SEC. 288. ILLEGAL PAYMENTS TO GOVERNMENT OFFICIALS OR EMPLOYEES.

(a) In General.—Paragraph (1) of section 162(c) (relating to illegal payments to Government officials or employees) is amended—

(1) by striking out "would be unlawful under the laws of the United States if such laws were applicable to such payment and to such official or employee" and inserting in lieu thereof "is unlawful under the Foreign Corrupt Practices Act of 1977", and

(2) by striking out "(or would be unlawful under the laws of the United States)" and inserting in lieu thereof "(or is unlawful under the Foreign Corrupt Practices Act of 1977)".

(b) Coordination With Subpart F—

(1) Subsection (a) of section 952 is amended by adding at the end thereof the following new sentence:

"The payments referred to in paragraph (4) are payments which would be unlawful under the Foreign Corrupt Practices Act of 1977 if the payor were a United States person."

(2) Subsection (a) of section 964 is amended by adding at the end thereof the following new sentence: "The payments referred to in the preceding sentence are payments which would be unlawful under the Foreign Corrupt Practices Act of 1977 if the payor were a United States person."

(c) Effective Date.—The amendments made by this section shall apply to payments made after the date of the enactment of this Act.

SEC. 289. DEBT MANAGEMENT PROVISIONS.

(a) Determination by Secretary of Investment Yield on United States Savings Bond.—

(1) Subsection (b) of section 22 of the Second Liberty Bond Act (31 U.S.C. 757c) is amended—

(A) by amending paragraph (3) to read as follows:

"(3) The Secretary of the Treasury, with the approval of the President, may fix the investment yield on any United States savings bond. The Secretary of the Treasury, with the approval of the President, may provide for increases and decreases in the investment yield on any outstanding United States savings bond; except that the investment yield on any bond for the period held may not be decreased below the minimum yield for such period guaranteed at the time of its issuance.";

(B) by striking out "the Secretary of the Treasury may prescribe: Provided" and all that follows down through the end of the second sentence of paragraph (1) of such subsection and inserting in lieu thereof "the Secretary of the Treasury may prescribe.";

(C) by striking out "and shall be expressed in terms of their maturity value" in the third sentence of paragraph (1) of such subsection; and

(D) by striking out "higher rates which are consistent" and inserting in lieu thereof "rates which are consistent" in subparagraph (B) of paragraph (2) of such subsection.

(2) The second sentence of section 22A(b)(1) of such Act is amended by striking out "the Secretary of the Treasury may prescribe" and all that follows down through the end thereof and inserting in lieu thereof "the Secretary of the Treasury may prescribe.".

(b) Transitional Rule.—In the case of any savings bond issued before the 30th day after the date of the enactment of this Act, for purposes of sections 22 and 22A of such Act, the minimum yield guaranteed for the period held shall be the scheduled investment yield for such period as in effect on such 30th day.

(c) Limit on Outstanding Bonds.—Effective on the date of the enactment of this Act, the last sentence of the second paragraph of the first section of the Second Liberty Bond Act (31 U.S.C. 752) is amended by striking out "$70,000,000,000" and inserting in lieu thereof "$110,000,000,000".

SEC. 290. JEFFERSON COUNTY MENTAL HEALTH CENTER.

(a) In General.—The Secretary is authorized and directed to pay, out of any money in the Treasury not otherwise appropriated, to the Jefferson County Mental Health Center, Incorporated, of Lakewood, Colorado, the sum of $50,000 in full settlement of all claims of the center against the United States for repayment of amounts the center erroneously refunded to its employees for social security contributions in the period after December 31, 1971, and prior to May 14, 1975, pursuant to instructions by the Internal Revenue Service.

(b) Limitation.—No part of the amount appropriated in subsection (a) in excess of 10 per centum shall be paid, delivered to, or received by any agent or attorney on account of services rendered in connection with this claim, and the same shall be unlawful, any

contract to the contrary notwithstanding. Any person violating the provisions of this subsection shall be guilty of a misdemeanor and, upon conviction thereof be fined any sum not exceeding $1,000.

SEC. 291. ALASKA NATIVE CORPORATIONS.

Paragraph (2) of subsection (d) of section 4994 of subpart B of chapter 45 (relating to windfall profit tax on domestic crude oil; categories of oil) is amended by striking "under" the first time it appears and inserting in lieu thereof "pursuant to".

SEC. 292. AWARDING OF COSTS AND CERTAIN FEES.

(a) IN GENERAL.—Subchapter B of chapter 76 (relating to proceedings by taxpayers and third parties) is amended by redesignating section 7430 as section 7431 and by inserting after section 7429 the following new section:

"SEC. 7430. AWARDING OF COURT COSTS AND CERTAIN FEES.

"(a) IN GENERAL.—In the case of any civil proceeding which is—

"(1) brought by or against the United States in connection with the determination, collection, or refund of any tax, interest, or penalty under this title, and

"(2) brought in a court of the United States (including the Tax Court),

the prevailing party may be awarded a judgment for reasonable litigation costs incurred in such proceeding.

"(b) LIMITATIONS.—

"(1) MAXIMUM DOLLAR AMOUNT.—The amount of reasonable litigation costs which may be awarded under subsection (a) with respect to any prevailing party in any civil proceeding shall not exceed $25,000.

"(2) REQUIREMENT THAT ADMINISTRATIVE REMEDIES BE EXHAUSTED.—A judgment for reasonable litigation costs shall not be awarded under subsection (a) unless the court determines that the prevailing party has exhausted the administrative remedies available to such party within the Internal Revenue Service.

"(3) ONLY COSTS ALLOCABLE TO THE UNITED STATES.—An award under subsection (a) shall be made only for reasonable litigation costs which are allocable to the United States and not to any other party to the action or proceeding.

"(4) EXCLUSION OF DECLARATORY JUDGMENT PROCEEDINGS.—

"(A) IN GENERAL.—No award for reasonable litigation costs may be made under subsection (a) with respect to any declaratory judgment proceeding.

"(B) EXCEPTION FOR SECTION 501(C)(3) DETERMINATION REVOCATION PROCEEDINGS.—Subparagraph (A) shall not apply to any proceeding which involves the revocation of a determination that the organization is described in section 501(c)(3).

"(c) DEFINITIONS.—For purposes of this section—

"(1) REASONABLE LITIGATION COSTS.—

"(A) IN GENERAL.—The term 'reasonable litigation costs' includes—

"(i) reasonable court costs,

"(ii) the reasonable expenses of expert witnesses in connection with the civil proceeding,

"(iii) the reasonable cost of any study, analysis, engineering report, test, or project which is found by the court to be necessary for the preparation of the party's case, and

"(iv) reasonable fees paid or incurred for the services of attorneys in connection with the civil proceeding.

"(B) Attorney's fees.—In the case of any proceeding in the Tax Court, fees for the services of an individual (whether or not an attorney) who is authorized to practice before the Tax Court shall be treated as fees for the services of an attorney.

"(2) Prevailing party.—

"(A) In general.—The term 'prevailing party' means any party to any proceeding described in subsection (a) (other than the United States or any creditor of the taxpayer involved) which—

"(i) establishes that the position of the United States in the civil proceeding was unreasonable, and

"(ii)(I) has substantially prevailed with respect to the amount in controversy, or

"(II) has substantially prevailed with respect to the most significant issue or set of issues presented.

"(B) Determination as to prevailing party.—Any determination under subparagraph (A) as to whether a party is a prevailing party shall be made—

"(i) by the court, or

"(ii) by agreement of the parties.

"(3) Civil actions.—The term 'civil proceeding' includes a civil action.

"(d) Multiple Actions.—For purposes of this section, in the case of—

"(1) multiple actions which could have been joined or consolidated, or

"(2) a case or cases involving a return or returns of the same taxpayer (including joint returns of married individuals) which could have been joined in a single proceeding in the same court,

such actions or cases shall be treated as one civil proceeding regardless of whether such joinder or consolidation actually occurs, unless the court in which such action is brought determines, in its discretion, that it would be inappropriate to treat such actions or cases as joined or consolidated for purposes of this section.

"(e) Right of Appeal.—An order granting or denying an award for reasonable litigation costs under subsection (a), in whole or in part, shall be incorporated as a part of the decision or judgment in the case and shall be subject to appeal in the same manner as the decision or judgment.

"(f) Termination.—This section shall not apply to any proceeding commenced after December 31, 1985."

(b) Penalty for Using Tax Court Proceedings for Delay: Penalty for Frivolous or Groundless Proceeding.—The first sentence of section 6673 (relating to damages assessable by instituting proceedings before the Tax Court merely for delay) is amended to read

as follows: "Whenever it appears to the Tax Court that proceedings before it have been instituted or maintained by the taxpayer primarily for delay or that the taxpayer's position in such proceedings is frivolous or groundless, damages in an amount not in excess of $5,000 shall be awarded to the United States by the Tax Court in its decision.".

(c) Application With Title 28.—Section 2412 of title 28, United States Code, is amended by adding at the end thereof the following new subsection:

"(e) The provisions of this section shall not apply to any costs, fees, and other expenses in connection with any proceeding to which section 7430 of the Internal Revenue Code of 1954 applies (determined without regard to subsections (b) and (f)). Nothing in the preceding sentence shall prevent the awarding under subsection (a) of section 2412 of title 28, United States Code, of costs enumerated in section 1920 of such title (as in effect on October 1, 1981).".

(d) Conforming Amendments.—

(1) The table of sections for subchapter B of chapter 76 is amended by striking out the item relating to section 7430 and inserting the following new items:

"Sec. 7430. Awarding of court costs and certain fees.
"Sec. 7431. Cross references.".

(2)(A) The section heading of section 6673 is amended by striking out "MERELY FOR DELAY." and inserting in lieu thereof "PRIMARILY FOR DELAY, ETC.".

(B) The table of sections for subchapter B of chapter 68 is amended by striking out "merely for delay." in the item relating to section 6673 and inserting in lieu thereof "primarily for delay, etc.".

(e) Effective Dates.—

(1) In general.—The amendments made by this section shall apply to civil actions or proceedings commenced after February 28, 1983.

(2) Penalty.—The amendments made by subsections (b) and (d)(2) shall apply to any action or proceeding in the Tax Court commenced after December 31, 1982,

SEC. 293. TREATMENT OF CERTAIN LENDING OR FINANCE BUSINESSES FOR PURPOSES OF THE TAX ON PERSONAL HOLDING COMPANIES.

(a) Removal of Limitation on Amount of Ordinary Gross Income From Lending or Finance Business Taken Into Account.—Clause (ii) of section 542(c)(6)(C) (relating to exceptions from definition of personal holding company) is amended by striking out "but not $1,000,000".

(b) Changes in Definition of Lending or Finance Business.—Clause (i) of section 542(d)(1)(B) (relating to exceptions from definition of lending or finance business) is amended to read as follows:

"(i) making loans, or purchasing or discounting accounts receivable, notes, or installment obligations, if (at the itme of the loan, purchase, or discount) the remaining maturity exceeds 144 months; unless—

"(I) the loans, notes, or installment obligations are evidenced or secured by contracts of conditional sale, chattel mortgages, or chattel lease agreements arising out of the sale of goods or services in

the course of the borrower's or transferor's trade or business, or

"(II) the loans, notes, or installment obligations are made or acquired by the taxpayer and meet the requirements of subparagraph (C), or".

(c) INDEFINITE MATURITY CREDIT TRANSACTIONS.—Paragraph (1) of section 542(d) (relating to special rules) is amended by adding at the end thereof the following new subparagraph:

"(C) INDEFINITE MATURITY CREDIT TRANSACTIONS.—For purposes of subparagraph (B)(i), a loan, note, or installment obligation meets the requirements of this subparagraph if it is made under an agreement—

"(i) under which the creditor agrees to make loans or advances (not in excess of an agreed upon maximum amount) from time to time to or for the account of the debtor upon request, and

"(ii) under which the debtor may repay the loan or advance in full or in installments."

(d) EFFECTIVE DATES.—

(1) SUBSECTION (a).—The amendment made by subsection (a) shall apply to taxable years beginning after December 31, 1981.

(2) SUBSECTIONS (b) and (c). The amendments made by subsections (b) and (c) shall apply to taxable years beginning after December 31, 1980.

SEC. 294. ADDITIONAL REFUNDS RELATING TO REPEAL OF EXCISE TAX ON BUSES.

(a) TIME FOR FILING CLAIM.—Subparagraph (C) of section 231(c)(2) of the Energy Tax Act of 1978 (relating to refunds with respect to certain consumer purchases) is amended by striking out "the first day of such 10th calendar month" and inserting in lieu thereof "December 31, 1982".

(b) PROCEDURE FOR PASSING THROUGH REFUND.—Subparagraph (A) of section 231(c)(2) of such Act is amended by inserting before the semicolon ", or, in lieu of evidence of reimbursement, he makes such reimbursement simultaneously with the receipt of such a refund under an arrangement satisfactory to such Secretary which assures such simultaneous reimbursement".

TITLE III—TAXPAYER COMPLIANCE

Subtitle A—Withholding on Interest and Dividends

SEC. 301. WITHHOLDING ON INTEREST AND DIVIDENDS.

Chapter 24 (relating to collection of income tax at source on wages) is amended by adding at the end thereof the following new subchapter:

"Subchapter B—Withholding From Interest and Dividends

"Sec. 3451. Income tax collected at source on interest, dividends, and patronage dividends.
"Sec. 3452. Exemptions from withholding.
"Sec. 3453. Payor defined.
"Sec. 3454. Definitions of interest, dividend, and patronage dividend.
"Sec. 3455. Other definitions and special rules.
"Sec. 3456. Administrative provisions.

"SEC. 3451. INCOME TAX COLLECTED AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.

"(a) REQUIREMENT OF WITHHOLDING.—Except as otherwise provided in this subchapter, the payor of any interest, dividend, or patronage dividend shall withhold a tax equal to 10 percent of the amount of the payment.

"(b) SPECIAL RULES.—

"(1) TIME OF WITHHOLDING.—Except as otherwise provided in this subchapter, for purposes of this subchapter—

"(A) any payment of interest, dividend, or patronage dividend shall be treated as made, and

"(B) the tax imposed by this section shall be withheld,

at the time such interest, dividend, or patronage dividend is paid or credited.

"(2) PAYEE UNKNOWN.—If a payor is unable to determine the person to whom any interest, dividend, or patronage dividend is payable or creditable, the tax under this section shall be withheld at the time withholding would be required under paragraph (1) if the payee were known and were an individual.

"(3) AMOUNT OF DIVIDEND, ETC., UNKNOWN.—

"(A) IN GENERAL.—If the payor is unable to determine the portion of a distribution which is a dividend, the tax under this section shall be computed on the gross amount of the distribution. To the extent provided in regulations, a similar rule shall apply in the case of interest and patronage dividends.

"(B) Distributions which are not dividends.—To the extent provided in regulations, this section shall not apply to the extent that the portion of a distribution which is not a dividend may reasonably be estimated.

"(4) Withholding from alternative source.—The Secretary shall prescribe regulations setting forth the circumstances under which the tax imposed by this section may be paid from an account or source other than the payment which gives rise to the liability for tax.

"(c) Liability for Payment.—

"(1) Payor liable.—Except as otherwise provided in this subchapter, the payor—

"(A) shall be liable for the payment of the tax imposed by this section which such payor is required to withhold under this section, and

"(B) shall not be liable to any person (other than the United States) for the amount of any such payment.

"(2) Reliance on exemption certificates.—The payor shall not be liable for the payment of tax imposed by this section which such payor is required to withhold under this section if—

"(A) such payor fails to withhold such tax, and

"(B) such failure is due to reasonable reliance on an exemption certificate delivered to such payor under section 3452(f) which is in effect with respect to the payee at the time such tax is required to be withheld under this section.

"SEC. 3452. EXEMPTIONS FROM WITHHOLDING.

"(a) In General.—Section 3451 shall not apply with respect to—

"(1) any payment to an exempt individual,

"(2) any payment to an exempt recipient,

"(3) any minimal interest payment, or

"(4) any qualified consumer cooperative payment.

"(b) Exempt Individuals.—

"(1) In general.—For purposes of this section, the term 'exempt individual' means any individual—

"(A) who is described in paragraph (2), and

"(B) with respect to whom an exemption certificate is in effect.

"(2) Individuals described in this paragraph.—An individual is described in this paragraph if—

"(A) such individual's income tax liability for the preceding taxable year did not exceed $600 ($1,000 in the case of a joint return under section 6013), or

"(B)(i) such individual is 65 or older, and

"(ii) such individual's income tax liability for the preceding taxable year did not exceed $1,500 ($2,500 in the case of a joint return under section 6013).

"(3) Special rule for married persons.—A husband and wife shall each be treated as satisfying the requirements of paragraph (2)(B)(i) if—

"(A) either spouse is 65 or older, and

"(B) such husband and wife made a joint return under section 6013 for the preceding taxable year.

"(4) SPECIAL RULE FOR CERTAIN TRUSTS DISTRIBUTING CURRENTLY.—Under regulations, a trust—

"(A) the terms of which provide that all of its income is required to be distributed currently, and

"(B) all the beneficiaries of which are individuals described in paragraph (2) or organizations described in subsection (c)(2)(B),

shall be treated as an individual described in paragraph (2).

"(5) INCOME TAX LIABILITY.—For purposes of this subsection, the term 'income tax liability' means the amount of the tax imposed by subtitle A for the taxable year, reduced by the sum of the credits allowable against such tax (other than credits allowable by sections 31, 39, and 43).

"(c) EXEMPT RECIPIENTS.—

"(1) IN GENERAL.—For purposes of this section, the term 'exempt recipient' means any person described in paragraph (2)—

"(A) with respect to whom an exemption certificate is in effect, or

"(B) who is described in regulations prescribed by the Secretary which permit exemption from withholding without cerification.

"(2) PERSONS DESCRIBED IN THIS PARAGRAPH.—A person is described in this paragraph if such person is—

"(A) a corporation,

"(B) an organization exempt from taxation under section 501(a) or an individual retirement plan,

"(C) the United States or a State,

"(D) a foreign government or international organization,

"(E) a foreign central bank of issue,

"(F) a dealer in securities or commodities required to register as such under the laws of the United States or a State,

"(G) a real estate investment trust (as defined in section 856),

"(H) an entity registered at all times during the taxable year under the Investment Company Act of 1940,

"(I) a common trust fund (as defined in section 584(a)),

"(J) a nominee or custodian (except as otherwise provided in regulations),

"(K) to the extent provided in regulations—

"(i) a financial institution,

"(ii) a broker, or

"(iii) any other person specified in such regulations, who collects any interest, dividend, or patronage dividend for the payee or otherwise acts as a middleman betwen the payor and payee, or

"(L) any trust which—

"(i) is exempt from tax under section 664(c), or

"(ii) is described in section 4947(a)(1).

"(3) PAYOR MAY REQUIRE CERTIFICATION.—A person described in paragraph (1)(B) shall not be treated as an exempt recipient for purposes of this section with respect to any payment of such payor if—

"(A) an exemption certificate is not in effect with respect to such person, and

"(B) the payor does not treat such person as an exempt recipient.

"(d) MINIMAL INTEREST PAYMENTS.—

"(1) IN GENERAL.—For purposes of this section, the term 'minimal interest payment' means any payment of interest—

"(A) with respect to which an election by the payor made under paragraph (3) is in effect, and

"(B) which—

"(i) does not exceed $150, and

"(ii) if determined for a 1-year period would not exceed $150.

"(2) AGGREGATION OF PAYMENTS TO SAME PAYEE.—To the extent provided in regulations prescribed by the Secretary, payments of interest by a payor to the same payee shall be aggregated for purposes of applying paragraph (1)(B).

"(3) ELECTION.—

"(A) IN GENERAL.—Any payor may make an election under this paragraph with respect to any type of interest payments.

"(B) EFFECTIVE UNTIL REVOKED.—Except as provided in regulations prescribed by the Secretary, an election made by any person under this paragraph shall remain in effect until revoked by such person.

"(C) TIME AND MANNER.—Any election or revocation of an election made under this paragraph shall be made at such time and in such manner as the Secretary shall prescribe by regulations.

"(e) QUALIFIED CONSUMER COOPERATIVE PAYMENT.—For purposes of this section, the term 'qualified consumer cooperative payment' means any payment by a cooperative which is exempt from reporting requirements under section 6044(a) by reason of section 6044(c).

"(f) EXEMPTION CERTIFICATES.—

"(1) IN GENERAL.—

"(A) DELIVERY.—An exempt individual or exempt recipient may deliver an exemption certificate to a payor at any time. Such certificate shall be in such form and contain such information as the Secretary shall prescribe.

"(B) CHANGE OF STATUS.—Any person who ceases to be an exempt individual or exempt recipient shall, not later than the close of the 10th day after the date of such cessation, notify each payor with whom such person has an exemption certificate of such change in status. No notice shall be required under the preceding sentence with respect to any payor if it reasonably appears that the person will not thereafter receive a payment of interest, dividends, or patronage dividends from such payor.

"(2) EFFECTIVENESS OF CERTIFICATES.—

"(A) GENERAL RULE.—Except as otherwise provided in regulations prescribed by the Secretary, an exemption certificate shall be effective until—

"(i) revoked, or

"(ii) notice of change in status is provided pursuant to paragraph (1)(B).

"(B) When certificate takes effect.—The Secretary shall prescribe regulations setting forth—

"(i) the day on which a filed exemption certificate shall be considered effective, and

"(ii) the circumstances under which a payor shall treat an exemption certificate as having ceased to be effective where the Secretary has determined that the person described therein is not an exempt individual or exempt recipient.

"SEC. 3453. PAYOR DEFINED.

"(a) General Rule.—Except as otherwise provided in this subchapter, for purposes of this subchapter, the term 'payor' means the person paying or crediting the interest, dividend, or patronage dividend.

"(b) Certain Middlemen Treated as Payors.—For purposes of this subchapter—

"(1) In general.—To the extent provided in regulations—

"(A) any custodian for, or nominee of, the payee,

"(B) any corporate trustee of a trust which is the payee, or

"(C) any person which collects the payment for the payee or otherwise acts as a middleman between the payor and the payee,

shall be treated as a payor with respect to the payment.

"(2) Receipt treated as payment.—To the extent provided in regulations, any person treated as a payor under paragraph (1) shall be treated as having paid the interest, dividend, or patronage dividend when such person received such amount.

"(c) Agents, Etc.—In the case of—

"(1) a fiduciary or agent with respect to the payment or crediting of any interest, dividend, or patronage dividend, or

"(2) any other person who has the control, receipt, custody, or disposal of, or pays or credits any interest, dividend, or patronage dividend for any payor,

the Secretary, under regulations prescribed by him, may designate such fiduciary, agent, or other person as a payor with respect to such payment or crediting for purposes of this subchapter.

"(d) Treatment of Persons to Whom Subsection (b) or (c) Applies.—Any person treated as a payor under subsection (b) or (c)—

"(1) shall perform such acts as are required of a payor (within the meaning of subsection (a)) and as may be specified by the Secretary, and

"(2) shall be treated as a payor for all provisions of law (including penalties) applicable in respect to a payor (within the meaning of subsection (a)).

"(e) Relief From Double Withholding.—The Secretary may by regulations provide that where any person is treated as a payor under subsection (b) or (c) with respect to any payment, any other person who (but for this subsection) would be treated as a payor with respect to such payment shall be relieved from the requirements of this subchapter to the extent provided in such regulations.

"(f) LIABILITY OF THIRD PARTIES PAYING OR PROVIDING INTEREST, DIVIDENDS, OR PATRONAGE DIVIDENDS.—To the extent provided in regulations prescribed by the Secretary, rules similar to the rules of section 3505 (relating to liability of third parties paying or providing for wages) shall apply for purposes of this subchapter. For purposes of the preceding sentence, the last sentence of subsection (b) of section 3505 shall be applied by substituting '10 percent' for '25 percent'.

"SEC. 3454. DEFINITIONS OF INTEREST, DIVIDEND, AND PATRONAGE DIVIDEND.

"(a) INTEREST DEFINED.—For purposes of this subchapter—

"(1) GENERAL RULE.—The term 'interest' means—

"(A) interest on any obligation in registered form or of a type offered to the public,

"(B) interest on deposits with persons carrying on the banking business,

"(C) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit union, industrial loan association or bank, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares,

"(D) interest on amounts held by an insurance company under an agreement to pay interest thereon,

"(E) interest on deposits with brokers (as defined in section 6045(c)), and

"(F) interest paid on amounts held by investment companies (as defined in section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3)) and on amounts invested in other pooled funds or trusts.

"(2) EXCEPTIONS.—The term 'interest' does not include—

"(A) interest on any obligation issued by a natural person,

"(B) interest on any obligation if such interest is exempt from taxation under section 103(a) or if such interest is exempt from tax (without regard to the identity of the holder) under any other provision of law,

"(C) any amount paid on a depository institution tax-exempt certificate (as defined in section 128(c)(1) (as in effect for taxable years beginning before January 1, 1985)),

"(D) any amount which is subject to withholding under subchapter A of chapter 3 (relating to withholding of tax on nonresident aliens and foreign corporations) by the person paying such amount,

"(E) any amount which would be subject to withholding under subchapter A of chapter 3 by the person paying such amount but for the fact that—

"(i) such amount is income from sources outside the United States,

"(ii) the payor thereof is excepted from the application of section 1441(a) by reason of section 1441(c) or a tax treaty, or

"(iii) such amount is original issue discount (within the meaning of section 1232(b)(1)),

"(F) any amount which is exempt from tax under—

"(i) section 892 (relating to income of foreign governments and of international organizations), or

"(ii) section 895 (relating to income derived by a foreign central bank of issue from obligations of the United States or from bank deposits),

"(G) except to the extent otherwise provided in regulations, any amount paid by—

"(i) a foreign government or international organization or any agency or instrumentality thereof,

"(ii) a foreign central bank of issue,

"(iii) a foreign corporation not engaged in trade or business in the United States,

"(iv) a foreign corporation, the interest payments of which would be exempt from withholding under subchapter A of chapter 3 if paid to a person who is not a United States person, or

"(v) a partnership not engaged in a trade or business in the United States and composed in whole of nonresident aliens, individuals and persons described in clause (i), (ii), or (iii),

"(H) any amount on which the person making payment is required to withhold a tax under section 1451 (relating to tax-free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions), and

"(I) except to the extent otherwise provided in regulations, any amount not described in the foregoing provisions of this paragraph which is paid outside the United States and is income from sources outside the United States.

"(3) ADJUSTMENT FOR PENALTY BECAUSE OF PREMATURE WITHDRAWAL OF FUNDS FROM TIME SAVINGS ACCOUNTS OR DEPOSITS.—To the extent provided in regulations, the amount of any interest on a time savings account, certificate of deposit, or similar class of deposits shall be appropriately reduced for purposes of this suchapter by the amount of any penalty imposed for the premature withdrawal of funds.

"(b) DIVIDEND DEFINED.—For purposes of this subchapter—

"(1) GENERAL RULE.—The term 'dividend' means—

"(A) any distribution by a corporation which is a dividend (as defined in section 316), and

"(B) any payment made by a stockbroker to any person as a substitute for a dividend (as so defined).

"(2) SUBCHAPTER S DISTRIBUTIONS AFTER CLOSE OF YEAR.—The term 'dividend' includes any distribution described in section 1375(f) (relating to distributions by electing small business corporations after the close of the taxable year).

"(3) EXCEPTIONS.—The term 'dividend' shall not include—

"(A) any amount paid as a distribution of stock described in section 305(e)(2)(A) (relating to reinvestment of dividends in stock of public utilities),

"(B) any amount which is treated as a taxable dividend by reason of section 302 (relating to redemptions of stock), 306 (relating to disposition of certain stock), 356 (relating to receipt of additional consideration in connection with certain reorganizations), or 1081(e)(2) (relating to certain distributions pursuant to order of the Securities and Exchange Commission),

"(C) any amount described in subparagraph (D), (E), or (F) of subsection (a)(2),

"(D) to the extent provided in regulations, any amount paid by a foreign corporation not engaged in a trade or business in the United States,

"(E) any amount which is a capital gain dividend distributed by—

"(i) a regulated investment company (as defined in section 852(b)(3)(C)), or

"(ii) a real estate investment trust (as defined in section 857(b)(3)(C)),

"(F) any amount which is an exempt-interest dividend of a regulated investment company (as defined in section 852(b)(5)(A)),

"(G) any amount paid or treated as paid by a regulated investment company during a year if, under regulations prescribed by the Secretary, it is anticipated that at least 95 percent of the dividends paid or treated as paid during such year (not including capital gain distributions) will be exempt-interest dividends, and

"(H) any amount described in section 1373 (relating to undistributed taxable income of electing small business corporations).

"(c) Patronage Dividend.—For purposes of this subchapter—

"(1) In general.—The term 'patronage dividend' means—

"(A) the amount of any patronage dividend (as defined in section 1388(a)) which is paid in money, qualified written notice of allocation, or other property (except a nonqualified written notice of allocation),

"(B) any amount, described in section 1382(c)(2)(A) (relating to certain nonpatronage distributions), which is paid in money, qualified written notice of allocation, or other property (except nonqualified written notice of allocation) by an organization exempt from tax under section 521 (relating to exemption of farmers' cooperatives from tax), and

"(C) any amount paid in money or other property (except written notice of allocation) in redemption of a nonqualified written notice of allocation attributable to any source described in subparagraph (A) or (B).

"(2) Exceptions.—The term 'patronage dividend' shall not include any amount described in subparagraph (D), (E), or (F) of subsection (a)(2).

"(3) Special rules.—In determining the amount of any patronage dividend—

"(A) property (other than a written notice of allocation) shall be taken into account at its fair market value.

"(B) a qualified written notice of allocation described in section 1388(c)(1)(A) shall be taken into account at its stated dollar amount, and

"(C) a patronage dividend part of which is a qualified written notice of allocation described in section 1388(c)(1)(B) (and not in section 1388(c)(1)(A)) shall be taken into account only if 50 percent or more of such dividend is paid in money or by a qualified check, and any such qualified written notice of allocation which is taken into account after the application of this subparagraph shall be taken into account at its stated dollar amount.

"(4) DEFINITIONS.—For purposes of this subsection—

"(A) QUALIFIED WRITTEN NOTICE OF ALLOCATION.—The term 'qualified written notice of allocation' has the meaning given to such term by section 1388(c).

"(B) NONQUALIFIED WRITTEN NOTICE OF ALLOCATION.—The term 'nonqualified written notice of allocaion' has the meaning given to such term by section 1388(d).

"(C) QUALIFIED CHECK.—The term 'qualified check' has the meaning given to such term by section 1388(c)(4).

"SEC. 3455. OTHER DEFINITIONS AND SPECIAL RULES.

"(a) DEFINITIONS.—For purposes of this subchapter—

"(1) PERSON.—The term 'person' includes any governmental unit and any agency or instrumentality thereof and any international organization.

"(2) STATE.—The term 'State' means a State, the District of Columbia, a possession of the United States, any political subdivision of any of the foregoing, and any wholly owned agency or instrumentality of any one or more of the foregoing.

"(3) UNITED STATES.—The term 'United States' means the United States and any wholly owned agency or instrumentality thereof.

"(4) FOREIGN GOVERNMENT.—The term 'foreign government' means a foreign government, a political subdivision of a foreign government, and any wholly owned agency or instrumentality of any one or more of the foregoing.

"(5) INTERNATIONAL ORGANIZATION.—The term 'international organization' means an international organization and any wholly owned agency or instrumentality thereof.

"(6) NONRESIDENT ALIEN.—The term 'nonresident alien individual' includes an alien resident of Puerto Rico.

"(7) WITHHOLD, ETC., INCLUDE DEDUCT.—The terms 'withhold', 'withholding', and 'withheld' include deduct, deducting, and deducted.

"(b) TREATMENT OF ORIGINAL ISSUE DISCOUNT.—

"(1) IN GENERAL.—Except as provided in paragraphs (2) and (3) the tax imposed by section 3451 shall apply to the amount of original issue discount on any obligation which is includible in the gross income of the holder during the calendar year. Any such amount shall be treated as a payment for purposes of this subchapter.

"(2) Transferred obligations.—

"(A) In general.—In the case of original issue discount on any obligation which has been transferred from the original holder, the tax imposed by section 3451 shall apply to such original issue discount as if the subsequent holder were the original holder.

"(B) Special rule for short-term obligations.—In the case of any obligation with a fixed maturity date not exceeding 1 year from the date of issue which has been transferred from the original holder, if any subsequent purchaser establishes the date on which, and the purchase price at which, he acquired such obligation, the amount of original issue discount on such obligation shall be determined (subject to such regulations as the Secretary may prescribe) as if it were issued on the date such subsequent purchaser acquired such obligation for an issue price equal to the purchase price at which such subsequent purchaser acquired such obligation.

"(3) Limitation on amount withheld.—

"(A) In general.—The amount of tax imposed by section 3451 on the original issue discount on any obligation which is required to be withheld under section 3451(a) in any calendar year shall not exceed the amount of cash paid with respect to such obligation during such calendar year.

"(B) Authority of secretary to eliminate limitation in certain cases.—If the Secretary determines by regulations that a type of obligation is frequently used to avoid the purposes of this subchapter, subparagraph (A) shall not apply with respect to original issue discount on any obligation of such type which is issued more than 30 days after the first date on which such regulations are published in the Federal Register.

"(C) Payments from which withholding is to be made.—Except to the extent otherwise provided in regulations, the tax imposed by section 3451 with respect to original issue discount for any calendar year shall be withheld from each cash payment made with respect to such obligation during such calendar year in the proportion which the amount of such payment bears to the aggregate of such payments.

"(4) Original issue discount defined.—For purposes of this subsection, the term 'original issue discount' has the meaning given such term by section 1232(b)(1).

"SEC. 3456. ADMINISTRATIVE PROVISIONS.

"(a) Return and Payment by Governmental Units.—If the payor of any payment subject to withholding under section 3451 is the United States or a State, or an agency or instrumentality thereof, the return of the tax withheld under this subchapter shall be made by the officer or employee having control of the payment of the amount subject to withholding or by any officer or employee appropriately designated to make such withholding.

"(b) Annual Withholding by Financial Institutions.—

"(1) In general.—Under regulations prescribed by the Secretary, a financial institution described in subparagraph (B) or

(C) of section 3454(a)(1) may elect to defer withholding of the tax imposed by section 3451 during any calendar year on interest paid on savings accounts, interest-bearing checking accounts, and similar accounts until a date which is not later than the last day of such year.

"(2) Condition for election.—The regulations prescribed under paragraph (1) shall provide that an election under such paragraph is conditional on agreement by the person making the election—

"(A) that the balance in any account subject to such election shall at no time be less than an amount equal to the tax under section 3451 which would have been withheld as of such time if such election were not in effect, and

"(B) that if an account subject to such election is closed before the date on which the tax under section 3451 would (but for this subparagraph) be withheld as a result of such an election, the tax shall be withheld before the time of closing such account.

"(c) Tax Paid by Recipient.—If a payor, in violation of the provisions of this subchapter, fails to withhold the tax imposed under section 3451, and thereafter the tax against which such tax may be credited is paid, the tax so required to be withheld shall not be collected from the payor; but this subsection shall in no case relieve the payor from liability for any penalties or additions to the tax otherwise applicable in respect of such failure to withhold.

"(d) Regulations.—The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subchapter."

SEC. 302. CREDIT AGAINST TAX.

(a) In General.—Section 31 (relating to tax withheld on wages) is amended to read as follows:

"SEC. 31. TAX WITHHELD ON WAGES, INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.

"(a) Wage Withholding.—The amount withheld under section 3402 as tax on the wages of any individual shall be allowed to the recipient of the income as a credit against the tax imposed by this subtitle.

"(b) Withholding From Interest, Dividends, and Patronage Dividends.—The amount withheld under section 3451 as tax on interest, dividends, and patronage dividends shall be allowed to the recipient of the income as a credit against the tax imposed by this subtitle.

"(c) Credit for Special Refunds of Social Security Tax.—The Secretary may prescribe regulations providing for the crediting against the tax imposed by this subtitle of the amount determined by the taxpayer or the Secretary to be allowable under section 6413(c) as a special refund of tax imposed on wages. The amount allowed as a credit under such regulations shall, for purposes of this subtitle, be considered an amount withheld at source as tax under section 3402.

"(d) Year for Which Credit Allowed.—

"(1) In general.—Except as otherwise provided in paragraph (2), any credit allowed by this section shall be allowed for the

taxable year beginning in the calendar year in which the amount was withheld (or, in the case of subsection (c), in which the wages were received). If more than 1 taxable year begins in a calendar year, such amount shall be allowed as a credit for the last taxable year so beginning.

"(2) SPECIAL RULE FOR CERTAIN DISTRIBUTIONS OF SUBCHAPTER S CORPORATIONS.—The amount withheld with respect to a distribution by an electing small business corporation (within the meaning of section 1371(b)) which is treated as a distribution of such corporation's undistributed taxable income for the preceding year under section 1375(f)(1) shall be allowed as a credit for the taxable year of the recipient beginning in the calendar year in which the preceding year of the corporation ends."

(b) TREATMENT OF ESTATES AND TRUSTS.—

(1) IN GENERAL.—Section 643 (relating to definitions applicable to estates and trustrs) is amended by adding at the end thereof the following new subsection:

"(d) COORDINATION WITH WITHHOLDING ON INTEREST AND DIVIDENDS.—Except to the extent otherwise provided in regulations, this subchapter shall be applied with respect to payments subject to withholding under subchapter B of chapter 24—

"(1) by allocating between the estate or trust and its beneficiaries any credit allowable under section 31(b) (on the basis of their respective shares of interest, dividends, and patronage dividends taken into account under this subchapter),

"(2) by treating each beneficiary to whom such credit is allocated as if an amount equal to such credit had been paid to him by the estate or trust, and

"(3) by allowing the estate or trust a deduction in an amount equal to the credit so allocated to beneficiaries."

(2) TECHNICAL AMENDMENT.—Subsection (a) of section 661 (relating to deduction for estates and trusts accumlating income or distributing corpus) is amended by adding at the end thereof the following new sentence: "For purposes of paragraph (1), the amount of distributable net income shall be computed without the deduction allowed by section 642(c)."

(c) CONFORMING AMENDMENT.—Paragraph (1) of section 6413(c) is amended by striking out "section 31(b)" and inserting in lieu thereof "section 31(c)".

SEC. 303. RETURNS REGARDING PAYMENTS OF DIVIDENDS AND PAYMENTS OF INTEREST.

(a) DIVIDENDS.—

(1) IN GENERAL.—Paragraph (1) of subsection 6042(a) (relating to returns regarding payments of dividends) is amended—

(A) by striking out "or" at the end of subparagraph (A),

(B) by inserting "or" at the end of subparagraph (B),

(C) by inserting after subparagraph (B) the following new subparagraph:

"(C) who is required to withhold tax under section 3451 on any payment of dividends,",

(D) by striking out the period at the end thereof, and

(E) by inserting the following at the end thereof ", and, in the case of a payment upon which tax is withheld, the amount of tax withheld."

(2) STATEMENTS.—Section 6042(c) (relating to statements to be furnished to persons with respect to whom information is furnished) is amended—

(A) by striking out "and" at the end of paragraph (1),

(B) by striking out the period at the end of paragraph (2) and inserting in lieu thereof ", and",

(C) by inserting after paragraph (2) the following paragraph:

"(3) the amount of tax withheld under section 3451.", and

(D) by striking out "No statement" in the last sentence thereof and inserting in lieu thereof "Except in the case of a return required by reason of subparagraph (C) of subsection (a)(1), no statement".

(3) DUPLICATE FILED WITH SECRETARY.—Section 6042 is amended by adding at the end thereof the following new subsection:

"(e) DUPLICATE OF SUBSECTION (c) STATEMENT MAY BE REQUIRED TO BE FILED WITH SECRETARY.—A duplicate of any statement made pursuant to subsection (c) which is required to set forth an amount withheld under section 3451 shall, when required by regulations prescribed by the Secretary, be filed with the Secretary."

(b) INTEREST.—Section 6049 (relating to returns regarding payments of interest) is amended by adding at the end thereof the following new subsection:

"(e) DUPLICATE OF SUBSECTION (c) STATEMENT MAY BE REQUIRED TO BE FILED WITH SECRETARY.—A duplicate of any statement made pursuant to subsection (c) which is required to set forth an amount withheld under section 3451 shall, when required by regulations prescribed by the Secretary, be filed with the Secretary."

SEC. 304. RETURNS REGARDING PAYMENTS OF PATRONAGE DIVIDENDS.

(a) IN GENERAL.—Paragraph (1) of subsection 6044(a) is amended to read as follows:

"(1) IN GENERAL.—Except as otherwise provided in this section, every cooperative to which part I of subchapter T of chapter 1 applies which—

"(A) makes payments of amounts described in subsection (b) aggregating $10 or more to any person during any calendar year, or

"(B) is required to withhold any tax under section 3451, shall make a return according to the forms or regulations prescribed by the Secretary, setting forth the aggregate amount of such payments, the name and address of the person to whom paid, and the amount of tax withheld."

(b) AMOUNTS SUBJECT TO REPORTING.—Paragraph (1) of section 6044(b) (relating to amounts subject to reporting) is amended by striking out "under subsection (a)", and by inserting "under paragraph (1)(A) or (2) of subsection (a)".

(c) STATEMENTS.—Section 6044(e) (relating to statements to be furnished to persons with respect to whom information is furnished) is amended—

(1) by striking out "and" at the end of paragraph (1),

(2) by striking out the period at the end of paragraph (2), and inserting ", and" in lieu thereof,

(3) by inserting after paragraph (2) the following paragraph: "(3) the amount of tax withheld under section 3451.", and

(4) by striking out "No statement" in the last sentence thereof and inserting in lieu thereof "Except in the case of a return required by reason of subparagraph (B) of subsection (a)(1), no statement".

(d) DUPLICATE FILED WITH SECRETARY.—Section 6044 is amended by adding at the end threof the following new subsection:

"(f) DUPLICATE OF SUBSECTION (e) STATEMENT MAY BE REQUIRED TO BE FILED WITH SECRETARY.—A duplicate of any statement made pursuant to subsection (e) which is required to set forth an amount withheld under section 3451 shall, when required by regulations prescribed by the Secretary, be filed with the Secretary."

SEC. 305. DENIAL OF DEDUCTION FOR CERTAIN TAXES.

(a) NO DEDUCTION FOR TAX WITHHELD AT SOURCE ON INTEREST, DIVIDENDS, AND PATRONAGE DIVIDENDS.—Paragraph (1) of section 275(a) (relating to denial of deduction for certain taxes) is amended—

(1) by striking out "and" at the end of subparagraph (B),

(2) by striking out the period at the end of subparagraph (C) and inserting in lieu thereof "; and", and

(3) by inserting after subparagraph (C) the following subparagraph:

"(D) the tax withheld at source on interest, dividends, and patronage dividends under section 3451."

(b) NO DEDUCTION OF TAXES WITHHELD ON INTEREST AND DIVIDENDS IN DETERMINING TAXABLE INCOME.—Subsection (b) of section 3502 (relating to the nondeductibility of taxes in computing taxable income) is amended—

(1) by striking out "under chapter 24" and inserting in lieu thereof "under subchapter A of chapter 24", and

(2) by adding at the end thereof the following new subsection:

"(c) The tax withheld under subchapter B of chapter 24 shall not be allowed as a deduction in computing taxable income under subtitle A either to the person withholding the tax or to the recipient of the amounts subject to withholding."

SEC. 306. PENALTIES.

(a) CIVIL PENALTY.—Paragraph (1) of section 6682(a) (relating to false information with respect to withholding) is amended by inserting "or section 3452(f)(1)(A)" after "section 3402".

(b) CRIMINAL PENALTY.—Section 7205 (relating to fraudulent withholding exemption certificate or failure to supply information) is amended—

(1) by striking out "Any individual" and inserting in lieu thereof "(a) WITHHOLDING ON WAGES.—Any individual", and

(2) by adding at the end thereof the following new subsection:

"(b) WITHHOLDING OF INTEREST AND DIVIDENDS.—Any person who—

"(1) willfully files an exemption certificate with any payor under section 3452(f)(1)(A), which is known by him to be fraudulent or to be false as to any material matter, or

"(2) is required to furnish notice under section 3452(f)(1(B), and willfully fails to furnish such notice in the manner and at the time required pursuant to section 3452(f)(1)(B) or the regulations prescribed thereunder,

shall, in lieu of any penalty otherwise provided, upon conviction thereof, be fined not more than $500, or imprisoned not more than 1 year, or both."

SEC. 307. CONFORMING AND CLERICAL AMENDMENTS.

(a) Conforming Amendments.—

(1) Paragraph (3) of section 274(e) (relating to disallowance of certain entertainment, etc., expenses) is amended by inserting "subchapter A of" before "chapter 24".

(2) Section 3403 (relating to liability for tax) is amended by striking out "this chapter" and inserting in lieu thereof "this subchapter".

(3) Paragraph (4) of section 3507(d) (relating to advance payment of earned income credit) is amended by inserting "subchapter A of" before "chapter 24".

(4) Subchapter (B) of section 6013(g)(1) (relating to joint returns of income tax by husband and wife) is amended by striking out "(relating to wage withholding)" and by inserting in lieu thereof "(relating to withholding on wages, interest, dividends, and patronage dividends)" and by striking out "of wages".

(5) Paragraph (1) of section 6013(h) is amended by striking out "(relating to wage withholding)" and inserting in lieu thereof "(relating to withholding on wages, interest, dividends, and patronage dividends)" and by striking out "of wages".

(6) Paragraph (1) of section 6015(j) (relating to declaration of estimated income tax by individuals) is amended by striking out ", as defined in section 3401(a)," and inserting in lieu thereof "(as defined in section 3401(a)) , or to the interest, dividends, and patronage dividends (as defined in section 3454),".

(7) Subparagraph (A) of section 6051(f)(1) (relating to receipts for employees) is amended by inserting "subchapter A of" before "chapter 24".

(8) Paragraph (2) of section 6365(c) (relating to definitions and special rules for purposes of the collection of State individual income taxes) is amended by inserting ", interest, dividends, and patronage dividends" before "paid on or after such date".

(9) Subsection (b) of section 6401 (relating to amounts treated as overpayments) is amended by inserting ", interest, dividends, and patronage dividends" after "tax withheld on wages".

(10) Paragraph (1) of section 6413(a) (relating to special credit and refund rules applicable to certain employment taxes) is amended by striking out "or 3402 is paid with respect to any payment of remuneration," and inserting in lieu thereof "3402 or 3451 is paid with respect to any payment of remuneration, interest, dividends, or other amounts,".

(11) Subsection (b) of section 6413 is amended—

(A) by striking from the heading of such subsection the words "OF CERTAIN EMPLOYMENT TAXES", and

(B) by striking out "or 3402 is paid or deducted with respect to any payment of remuneration" and inserting in lieu thereof "3402 or 3451 is paid or deducted with respect to any payment of remuneration, interest, dividends, or other amount".

(12) The heading for section 6413 is amended to read as follows:

"SEC. 6413. SPECIAL RULES APPLICABLE TO CERTAIN TAXES UNDER SUBTITLE C."

(13) The table of sections for subchapter B of chapter 65 is amended by striking out the item relating to section 6413 and inserting in lieu thereof the following:

"Sec. 6413. Special rules applicable to certain taxes under subtitle C."

(14) Subsections (e)(1) and (g)(3) of section 6654 (relating to failure by individuals to pay estimated income tax) are amended by inserting ", interest, dividends, and patronage dividends" after "tax withheld at source on wages".

(15) The last sentence of section 7215(b) (relating to offenses with respect to collected taxes) is amended to read as follows: "For purposes of paragraph (2), a lack of funds existing immediately after the payment of wages or amounts subject to withholding under subchapter B of chapter 24 (whether or not created by the payment of such wages or amounts) shall not be considered to be circumstances beyond the control of a person."

(16) Subsection (d) of section 7654 (relating to coordination of United States and Guam individual income taxes) is amended by inserting "subchapter A of" before "chapter 24".

(17) Section 7701(a)(16) (defining the term "withholding agent") is amended by striking out "or 1461" and inserting in lieu thereof "1461 or 3451".

(b) CLERICAL AMENDMENTS.—

(1) The heading of subtitle C is amended to read as follows:

"Subtitle C—Employment Taxes and Collection of Income Tax at Source".

(2) The table of subtitles for the Internal Revenue Code of 1954 is amended by striking out the item relating to subtitle C and inserting in lieu thereof the following:

"SUBTITLE C. Employment taxes and collection of income tax at source."

(3) The table of sections for subpart A of part IV of subchapter A of chapter 1 is amended by striking out the item relating to section 31 and inserting in lieu thereof the following:

"Sec. 31. Tax withheld on wages, interest, dividends, and patronage dividends."

(4) Chapter 24 is amended by striking out the chapter heading and inserting in lieu thereof the following:

“CHAPTER 24—COLLECTION OF INCOME TAX AT SOURCE

“SUBCHAPTER A. Withholding from wages.
“SUBCHAPTER B. Withholding from interest and dividends.

“Subchapter A—Withholding From Wages”.

(5) the heading for chapter 25 is amended to read as follows:

“CHAPTER 25—GENERAL PROVISIONS RELATING TO EMPLOYMENT TAXES AND COLLECTION OF INCOME TAXES AT SOURCE”.

(6) The table of chapters for subtitle C is amended by striking out the items relating to chapters 24 and 25 and inserting in lieu thereof the following:

“CHAPTER 24. Collection of income tax at source.
“CHAPTER 25. General provisions relating to employment taxes and collection of income taxes at source.”

SEC. 308. EFFECTIVE DATES; SPECIAL RULES.

(a) IN GENERAL.—Except as otherwise provided in this section, the amendments made by this part shall apply to payments of interest, dividends, and patronage dividends paid or credited after June 30, 1983.

(b) DELAY IN APPLICATION TO CERTAIN PAYORS.—The Secretary of the Treasury shall prescribe such regulations which delay (but not beyond December 31, 1983) the application of some or all of the provisions of subchapter B of chapter 24 of the Internal Revenue Code of 1954 to any payor until such time as such payor is able to comply without undue hardship with the requirements of such provisions.

(c) TEMPORARY RULE FOR CERTAIN WITHHOLDING EXEMPTIONS.—Until regulations are prescribed by the Secretary of the Treasury or his delegate under section 3452(c)(1)(B) of the Internal Revenue Code of 1954 (as added by this part), the payor may treat any person whose name reasonably indicates that such person is described in paragraph (2) of section 3452(c) of such Code (other than subparagraph (J) or (K) thereof) as an exempt recipient.

(d) DELAY IN MAKING DEPOSITS.—The time for making deposits under section 6302 of the Internal Revenue Code of 1954 of the tax imposed by section 3451 of such Code which is withheld by any person shall, to the extent provided in regulations, take into account the cost to such person of instituting a withholding system in order to comply with subchapter B of chapter 24 of such Code.

Subtitle B—Improved Information Reporting

PART I—EXPANDED REPORTING

SEC. 309. REPORTING OF INTEREST.

(a) GENERAL RULE.—Section 6049 (relating to returns regarding payments of interest) is amended to read as follows:

"SEC. 6049. RETURNS REGARDING PAYMENTS OF INTEREST.

"(a) REQUIREMENT OF REPORTING.—Every person—

"(1) who makes payments of interest (as defined in subsection (b)) aggregating $10 or more to any other person during any calendar year,

"(2) who receives payments of interest (as so defined) as a nominee and who makes payments aggregating $10 or more during any calendar year to any other person with respect to the interest so received, or

"(3) who is required under subchapter B of chapter 24 to withhold tax on the payment of any interest,

shall make a return according to the forms or regulations prescribed by the Secretary, setting forth the aggregate amount of such payments, tax deducted and withheld, and the name and address of the person to whom paid or from whom withheld.

"(b) INTEREST DEFINED.—

"(1) GENERAL RULE.—For purposes of subsection (a), the term 'interest' means—

"(A) interest on any obligation—

"(i) issued in registered form, or

"(ii) of a type offered to the public,

other than any obligation with a maturity (at issue) of not more than 1 year which is held by a corporation,

"(B) interest on deposits with persons carrying on the banking business,

"(C) amounts (whether or not designated as interest) paid by a mutual savings bank, savings and loan association, building and loan association, cooperative bank, homestead association, credit union, industrial loan association or bank, or similar organization, in respect of deposits, investment certificates, or withdrawable or repurchasable shares,

"(D) interest on amounts held by an insurance company under an agreement to pay interest thereon,

"(E) interest on deposits with brokers (as defined in section 6045 (c)),

"(F) interest paid on amounts held by investment companies (as defined in section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3)) and on amounts invested in other pooled funds or trusts, and

"(G) to the extent provided in regulations prescribed by the Secretary, any other interest (which is not described in paragraph (2)).

"(2) EXCEPTIONS.—For purposes of subsection (a), the term 'interest' does not include—

"(A) interest on any obligation issued by a natural person,

"(B) interest on any obligation if such interest is exempt from tax under section 103(a) or if such interest is exempt from tax (without regard to the identity of the holder) under any other provision of law,

"(C) except to the extent otherwise provided in regulations—

"(i) any amount paid to any person referred to in paragraph (2) of section 3452(c) (other than subparagraphs (J) and (K) thereof), or

"(ii) any amount described in section 3454(a)(2)(D) or (E),

"(D) except to the extent otherwise provided in regulations, any amount not described in subparagraph (C) of this paragraph which is income from sources outside the United States or which is paid by—

"(i) a foreign government or international organization or any agency or instrumentality thereof,

"(ii) a foreign central bank of issue,

"(iii) a foreign corporation not engaged in a trade or business in the United States,

"(iv) a foreign corporation, the interest payments of which would be exempt from withholding under subchapter A of chapter 3 if paid to a person who is not a United States person, or

"(v) a partnership not engaged in a trade or business in the United States and composed in whole of nonresident alien individuals and persons described in clause (i), (ii), or (iii), and

"(E) any amount on which the person making payment is required to deduct and withhold a tax under section 1451 (relating to tax-free covenant bonds), or would be so required but for section 1451(d) (relating to benefit of personal exemptions).

"(3) PAYMENTS BY UNITED STATES NOMINEES ETC., OF UNITED STATES PERSON.—If, within the United States, a United States person—

"(A) collects interest (or otherwise acts as a middleman between the payor and payee) from a foreign person described in paragraph (2)(D) or collects interest from a United States person which is income from sources outside the United States for a second person who is a United States person, or

"(B) makes payments of such interest to such second United States person,

notwithstanding paragraph (2)(D), such payment shall be subject to the requirements of subsection (a) with respect to such second United States person.

"(c) STATEMENTS TO BE FURNISHED TO PERSONS WITH RESPECT TO WHOM INFORMATION IS FURNISHED.—

"(1) IN GENERAL.—Every person making a return under subsection (a) shall furnish to each person whose name is set forth in such return a written statement showing—

"(A) the name and address of the person making such return,

"(B) the aggregate amount of payments to, or the aggregate amount includible in the gross income of, the person as shown on such return, and

"(C) the aggregate amount of tax deducted and withheld with respect to such person under subchapter B of chapter 24.

"(2) STATEMENT MUST BE FURNISHED ON OR BEFORE JANUARY 31.—The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) was made.

"(3) NO STATEMENT REQUIRED WHERE INTEREST IS LESS THAN $10.—No statement with respect to payments of interest to any person shall be required to be furnished to any person under this subsection if the aggregate amount of payments to such person shown on the return made with respect to paragraph (1) or (2), as the case may be, of subsection (a) is less than $10.

"(d) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) PERSON.—The term 'person' includes any governmental unit and any agency or instrumentality thereof and any international organization and any agency or instrumentality thereof.

"(2) OBLIGATION.—The term 'obligation' includes bonds, debentures, notes, certificates, and other evidences of indebtedness.

"(3) PAYMENTS BY GOVERNMENTAL UNITS.—In the case of payments made by any governmental unit or any agency or instrumentality thereof, the officer or employee having control of the payment of interest (or the person appropriately designated for purposes of this section) shall make the returns and statements required by this section.

"(4) FINANCIAL INSTITUTIONS, BROKERS, ETC., COLLECTING INTEREST MAY BE SUBSTITUTED FOR PAYOR.—To the extent and in the manner provided by regulations, in the case of any obligation—

"(A) a financial institution, broker, or other person specified in such regulations which collects interest on such obligation for the payee (or otherwise acts as a middleman between the payor and the payee) shall comply with the requirements of subsections (a) and (c), and

"(B) no other person shall be required to comply with the requirements of subsections (a) and (c) with respect to any interest on such obligation for which reporting is required pursuant to subparagraph (A).

"(5) INTEREST ON CERTAIN OBLIGATIONS MAY BE TREATED ON A TRANSACTIONAL BASIS.—

"(A) IN GENERAL.—To the extent and in the manner provided in regulations, this section shall apply with respect to—

"(i) any person described in paragraph (4)(A), and

"(ii) in the case of any United States savings bonds, any Federal agency making payments thereon,

on any transactional basis rather than on an annual aggregation basis.

"(B) SEPARATE RETURNS AND STATEMENTS.—If subparagraph (A) applies to interest on any obligation, the return under subsection (a) and the statement furnished under subsection (c) with respect to such transaction may be made separately, but any such statement shall be furnished to the payee at such time as the Secretary may prescribe by regula-

tions but not later than January 31 of the next calendar year.

"(C) STATEMENT TO PAYEE REQUIRED IN CASE OF TRANSACTIONS INVOLVING $10 OR MORE.—In the case of any transaction to which this paragraph applies which involves the payment of $10 or more of interest, a statement of the transaction may be provided to the payee of such interest in lieu of the statement required under subsection (c). Such statement shall be provided during January of the year following the year in which such payment is made.

"(6) TREATMENT OF ORIGINAL ISSUE DISCOUNT.—

"(A) IN GENERAL.—Original issue discount on any obligation shall be reported—

"(i) as if paid at the time it is includible in gross income under section 1232A (except that for such purpose the amount reportable with respect to any subsequent holder shall be determined as if he were the original holder), and

"(ii) if section 1232A does not apply to the obligation, at maturity (or, if earlier, on redemption).

In the case of any obligation not in registered form issued before January 1, 1983, clause (ii) and not clause (i) shall apply.

"(B) ORIGINAL ISSUE DISCOUNT.—For purposes of this paragraph, the term 'original issue discount' has the meaning given to such term by section 1232(b)(1).".

(b) TECHNICAL AMENDMENTS.—

(1) Subsection (a) of section 6041 (relating to information at source) is amended—

(A) by striking out "6049(a)(1)" and inserting in lieu thereof "6049(a)", and

(B) by striking out "6045, 6049(a)(2), or 6049(a)(3)" and inserting in lieu thereof "or 6045".

(2) Subsection (b) of section 6652 (relating to failure to file certain information returns) is amended by adding "or" at the end of paragraph (1) and by striking out paragraphs (3) and (4).

(3) Paragraph (1) of section 6678 is amended by striking out "6049(a)(1)" and inserting in lieu thereof "6049(a)".

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts paid (or treated as paid) after December 31, 1982.

SEC. 310. OBLIGATIONS REQUIRED TO BE REGISTERED.

(a) UNITED STATES OBLIGATIONS.—The Second Liberty Bond Act is amended by adding at the end thereof the following new section:

"SEC. 28. (a) Every registration-required obligation of the United States (or of any agency or instrumentality thereof) shall be in registered form.

"(b) For purposes of this section—

"(1) Except as provided in paragraph (2), the term 'registration-required obligation' means any obligation other than an obligation which—

"(A) is not of a type offered to the public, or

"(B) has a maturity (at issue) of not more than 1 year.

"(2) The term 'registration-required obligation' shall not include any obligation if—

"(A) there are arrangements reasonably designed to ensure that such obligation will be sold (or resold in connection with the original issue) only to a person who is not a United States person, and

"(B) in the case of an obligation not in registered form—

"(i) interest on such obligation is payable only outside the United States and its possessions, and

"(ii) on the face of such obligation there is a statement that any United States person who holds such obligation will be subject to limitations under the United States income tax laws.

"(c)(1) For purposes of subsection (a), a book entry obligation shall be treated as in registered form if the right to principal of, and stated interest on, such obligation may be transferred only through a book entry consistent with regulations prescribed by the Secretary of the Treasury.

"(2) The Secretary of the Treasury shall prescribe such regulations as may be necessary to carry out the purpose of subsection (a) where there is a nominee or chain of nominees.".

(b) OTHER OBLIGATIONS.—

(1) OBLIGATIONS MUST BE IN REGISTERED FORM TO BE TAX-EXEMPT.—Section 103 (relating to interest on certain governmental obligations) is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:

"(j) OBLIGATIONS MUST BE IN REGISTERED FORM TO BE TAX-EXEMPT.—

"(1) IN GENERAL.—Nothing in subsection (a) or in any other provision of law shall be construed to provide an exemption from Federal income tax for interest on any registration-required obligation unless the obligation is in registered form.

"(2) REGISTRATION-REQUIRED OBLIGATION.—The term 'registration-required obligation' means any obligation other than an obligation which—

"(A) is not of a type offered to the public,

"(B) has a maturity (at issue) of not more than 1 year, or

"(C) is described in section 163(f)(2)(B).

"(3) SPECIAL RULES.—

"(A) BOOK ENTRIES PERMITTED.—For purposes of paragraph (1), a book entry obligation shall be treated as in registered form if the right to the principal of, and stated interest on, such obligation may be transferred only through a book entry consistent with regulations prescribed by the Secretary.

"(B) NOMINEES.—The Secretary shall prescribe such regulations as may be necessary to carry out the purpose of paragraph (1) where there is a nominee or chain of nominees."

(2) DENIAL OF DEDUCTION FOR INTEREST IF OBLIGATION NOT IN REGISTERED FORM.—Section 163 (relating to deduction for interest) is amended by redesignating subsection (f) as subsection (g)

and by inserting after subsection (e) the following new subsection:

"(f) DENIAL OF DEDUCTION FOR INTEREST ON CERTAIN OBLIGATIONS NOT IN REGISTERED FORM.—

"(1) IN GENERAL.—Nothing in subsection (a) or in any other provision of law shall be construed to provide a deduction for interest on any registration-required obligation unless such obligation is in registered form.

"(2) REGISTRATION-REQUIRED OBLIGATION.—For purposes of this section—

"(A) IN GENERAL.—The term 'registration-required obligation' means any obligation (including any obligation issued by a governmental entity) other than an obligation which—

"(i) is issued by a natural person,

"(ii) is not of a type offered to the public,

"(iii) has a maturity (at issue) of not more than 1 year, or

"(iv) is described in subparagraph (B).

"(B) CERTAIN OBLIGATIONS NOT INCLUDED.—An obligation is described in this subparagraph if—

"(i) there are arrangements reasonably designed to ensure that such obligation will be sold (or resold in connection with the original issue) only to a person who is not a United States person, and

"(ii) in the case of an obligation not in registered form—

"(I) interest on such obligation is payable only outside the United States and its possessions, and

"(II) on the face of such obligation there is a statement that any United States person who holds such obligation will be subject to limitations under the United States income tax laws.

"(C) AUTHORITY TO INCLUDE OTHER OBLIGATIONS.—Clauses (ii) and (iii) of subparagraph (A), and subparagraph (B), shall not apply to any obligation if—

"(i) such obligation is of a type which the Secretary has determined by regulations to be used frequently in avoiding Federal taxes, and

"(ii) such obligation is issued after the date on which the regulations referred to in clause (i) take effect.

"(3) BOOK ENTRIES PERMITTED, ETC.—For purposes of this subsection, rules similar to the rules of section 103(j)(3) shall apply."

(3) DENIAL OF EARNINGS AND PROFITS ADJUSTMENT FOR INTEREST ON REGISTRATION-REQUIRED OBLIGATIONS NOT IN REGISTERED FORM.—Section 312 (relating to earnings and profits) is amended by adding at the end thereof the following new subsection:

"(m) NO ADJUSTMENT FOR INTEREST PAID ON CERTAIN REGISTRATION-REQUIRED OBLIGATIONS NOT IN REGISTERED FORM.—The earnings and profits of any corporation shall not be decreased by any interest with respect to which a deduction is not or would not be allowable by reason of section 163(f), unless at the time of issuance the issuer is a foreign corporation that is not a controlled foreign corpo-

ration (within the meaning of section 957), a foreign investment company (within the meaning of section 1246(b)), or a foreign personal holding company (within the meaning of section 552) and the issuance did not have as a purpose the avoidance of section 163(f) or this subsection".

(4) EXCISE TAX ON ISSUERS OF REGISTRATION-REQUIRED OBLIGATIONS WHICH ARE NOT IN REGISTERED FORM.—

(A) IN GENERAL.—Subtitle D (relating to miscellaneous excise taxes) is amended by adding after chapter 38 the following new chapter:

"CHAPTER 39—REGISTRATION-REQUIRED OBLIGATIONS

"Sec. 4701. Tax on issuer of registration-required obligation not in registered form.

"SEC. 4701. TAX ON ISSUER OF REGISTRATION-REQUIRED OBLIGATION NOT IN REGISTERED FORM.

"(a) IMPOSITION OF TAX.—In the case of any person who issues a registration-required obligation which is not in registered form, there is hereby imposed on such person on the issuance of such obligation a tax in an amount equal to the product of—

"(1) 1 percent of the principal amount of such obligation, multiplied by

"(2) the number of calendar years (or portions thereof) during the period beginning on the date of issuance of such obligation and ending on the date of maturity.

"(b) DEFINITIONS.—For purposes of this section—

"(1) REGISTRATION-REQUIRED OBLIGATION.—The term 'registration-required obligation' has the same meaning as when used in section 163(f), except that such term shall not include any obligation required to be registered under section 103(j).

"(2) REGISTERED FORM.—The term 'registered form' has the same meaning as when used in section 163(f)."

(B) CONFORMING AMENDMENT.—The table of chapters for subtitle D is amended by inserting after chapter 38 the following:

"CHAPTER 39. Registration-required obligations."

(5) DENIAL OF DEDUCTION FOR LOSSES ON CERTAIN OBLIGATIONS NOT IN REGISTERED FORM.—Section 165 (as amended by this Act) is amended by redesignating subsection (j) as subsection (k) and by inserting after subsection (i) the following new subsection:

"(j) DENIAL OF DEDUCTION FOR LOSSES ON CERTAIN OBLIGATIONS NOT IN REGISTERED FORM.—

"(1) IN GENERAL.—Nothing in subsection (a) or in any other provision of law shall be construed to provide a deduction for any loss sustained on any registration-required obligation unless such obligation is in registered form (or the issuance of such obligation was subject to tax under section 4701).

"(2) DEFINITIONS.—For purposes of this subsection—

"(A) REGISTRATION-REQUIRED OBLIGATION.—The term 'registration-required obligation' has the meaning given to

such term by section 163(f)(2) except that clause (iv) of subparagraph (A), and subparagraph (B), of such section shall not apply.

"(B) Registered form.—The term 'registered form' has the same meaning as when used in section 163(f).

"(3) Exceptions.—The Secretary may, by regulations, provide that this subsection and subsection (d) of section 1232 shall not apply with respect to obligations held by any person if—

"(A) such person holds such obligations in connection with a trade or business outside the United States,

"(B) such person holds such obligations as a broker dealer (registered under Federal or State law) for sale to customers in the ordinary course of his trade or business,

"(C) such person complies with reporting requirements with respect to ownership, transfers, and payments as the Secretary may require, or

"(D) such person promptly surrenders the obligation to the issuer for the issuance of a new obligation in registered form,

but only if such obligations are held under arrangements provided in regulations or otherwise which are designed to assure that such obligations are not delivered to any United States person other than a person described in subparagraph (A), (B), or (C)."

(6) Denial of capital gain treatment for gains on certain obligations not in registered form.—Section 1232 (relating to bonds and other evidences of indebtedness) is amended by redesignating subsection (d) as subsection (e) and by inserting after subsection (c) the following new subsection:

"(d) Denial of Capital Gain Treatment for Gains on Certain Obligations Not in Registered Form.—

"(1) In general.—If any registration-required obligation is not in registered form, any gain on the sale or other disposition of such obligation shall be treated as ordinary income (unless the issuance of such obligation was subject to tax under section 4701).

"(2) Definitions.—For purposes of this subsection—

"(A) Registration-required obligation.—The term 'registration-required obligation' has the meaning given to such term by section 163(f)(2) except that clause (iv) of subparagraph (A), and subparagraph (B), of such section shall not apply.

"(B) Registered form.—The term 'registered form' has the same meaning as when used in section 163(f)."

(c) Technical Amendments.—

(1) Subparagraph (A) of section 103(b)(4) (relating to certain exempt activities) is amended by striking out "if each obligation issued pursuant to the issue is in registered form and".

(2)(A) Paragraph (1) of section 103(h) (relating to certain obligations must be in registered form and not guaranteed or subsidized under an energy program) is amended by striking out subparagraph (A) and by redesignating subparagraphs (B) and (C) as subparagraphs (A) and (B), respectively.

*(B) The subsection heading for subsection (h) of section 103 is amended by striking out "*Must Be in Registered Form and Not*" and inserting in lieu thereof "*Must Not Be*".*

(3)(A) Subsection (j) of section 103A (relating to other requirements) is amended by striking out paragraph (1) and by redesignating paragraphs (2) and (3) as paragraphs (1) and (2), respectively.

(B) Subparagraph (B) of section 103A(c)(2) (defining qualified mortgage issue) is amended by striking out "and (f) and paragraphs (2) and (3) of subsection (j)" and inserting in lieu thereof "(f), and (j)".

(C) Subparagraph (C) of section 103A(c)(2) is amended by striking out ", and paragraph (1) of subsection (j)".

(D) Subparagraph (C) of section 103A(c)(3) (defining qualified veterans' mortgage bond) is amended by striking out "subsection (j)(2)" and inserting in lieu thereof "subsection (j)(1)".

(4) Subparagraph (A) of section 103A(c)(3) (defining qualified veterans' mortgage bond) is amended by striking out "in registered form".

(d) Effective Dates.—

(1) In general.—Except as otherwise provided in this subsection, the amendments made by this section shall apply to obligations issued after December 31, 1982.

(2) Long-term U.S. obligations.—The amendment made by subsection (a) shall apply to obligations issued after the date of the enactment of this Act under the first section of the Second Liberty Bond Act.

(3) Exception for certain warrants, etc.—The amendments made by subsection (b) shall not apply to any obligations issued after December 31, 1982, on the exercise of a warrant for the conversion of a convertible obligation if such warrant or obligation was offered or sold outside the United States without registration under the Securities Act of 1933 and was issued before August 10, 1982. A rule similar to the rule of the preceding sentence shall also apply in the case of any regulations issued under section 163(f)(2)(C) of the Internal Revenue Code of 1954 (as added by this section) except that the date on which such regulations take effect shall be substituted for "August 10, 1982".

SEC. 311. RETURNS OF BROKERS.

(a) General Rule.—

(1) Returns.—Section 6045 (relating to returns of brokers) is amended to read as follows:

"SEC. 6045. RETURNS OF BROKERS.

"(a) General Rule.—Every person doing business as a broker shall, when required by the Secretary, make a return, in accordance with such regulations as the Secretary may prescribe, showing the name and address of each customer, with such details regarding gross proceeds and such other information as the Secretary may by forms or regulations require with respect to such business.

"(b) Statements To Be Furnished to Customers.—Every person making a return under subsection (a) shall furnish to each customer

whose name is set forth in such return a written statement showing—

"(1) the name and address of the person making such return, and

"(2) the information shown on such return with respect to such customer.

The written statement required under the preceding sentence shall be furnished to the customer on or before January 31 of the year following the calendar year for which the return under subsection (a) was made.

"(c) DEFINITIONS.—For purposes of this section—

"(1) BROKER.—The term 'broker' includes—

"(A) a dealer,

"(B) a barter exchange, and

"(C) any other person who (for a consideration) regularly acts as a middleman with respect to property or services.

"(2) CUSTOMER.—The term 'customer' means any person for whom the broker has transacted any business.

"(3) BARTER EXCHANGE.—The term 'barter exchange' means any organization of members providing property or services who jointly contract to trade or barter such property or services."

(2) PENALTY.—Paragraph (1) of section 6678 (relating to penalty for failure to furnish certain statements) is amended—

(A) by inserting "6045(b)," after "6044(e),", and

(B) by inserting "6045(a)," after "6044(a)(1),".

(b) BARTER EXCHANGE TREATED AS THIRD-PARTY RECORDKEEPER.—Paragraph (3) of section 7609(a) (defining third-party recordkeeper) is amended by striking out "and" at the end of subparagraph (E), by striking out the period at the end of subparagraph (F) and inserting in lieu thereof "; and", and by adding at the end thereof the following new subparagraph:

"(G) any barter exchange (as defined in section 6045(c)(3))."

(c) EFFECTIVE DATES.—

(1) SUBSECTION (a).—The amendments made by subsection (a) shall take effect on the date of the enactment of this Act, except that—

(A) regulations relating to reporting by commodities and securities brokers shall be issued under section 6045 of the Internal Revenue Code of 1954 (as amended by this Act) within 6 months after the date of the enactment of this Act, and

(B) such regulations shall not apply to transactions occurring before January 1, 1983.

(2) SUBSECTION (b).—The amendments made by subsection (b) shall apply to summonses served after December 31, 1982.

SEC. 312. INFORMATION REPORTING REQUIREMENTS FOR PAYMENTS OF REMUNERATION FOR SERVICES AND DIRECT SALES.

(a) GENERAL RULE.—Subpart B of part III of subchapter A of chapter 61 (relating to information concerning transactions with other persons) is amended by inserting after section 6041 the following new section:

"SEC. 6041A. RETURNS REGARDING PAYMENTS OF REMUNERATION FOR SERVICES AND DIRECT SALES.

"(a) RETURNS REGARDING REMUNERATION FOR SERVICES.—If—

"(1) any service-recipient engaged in a trade or business pays in the course of such trade or business during any calendar year remuneration to any person for services performed by such person, and

"(2) the aggregate of such remuneration paid to such person during such calendar year is $600 or more,

then the service-recipient shall make a return, according to the forms or regulations prescribed by the Secretary, setting forth the aggregate amount of such payments and the name and address of the recipient of such payments. For purposes of the preceding sentence, the term 'service-recipient' means the person for whom the service is performed.

"(b) DIRECT SALES OF $5,000 OR MORE.—

"(1) IN GENERAL.—If—

"(A) any person engaged in a trade or business in the course of such trade or business during any calendar year sells consumer products to any buyer on a buy-sell basis, a deposit-commission basis, or any similar basis which the Secretary prescribes by regulations, for resale (by the buyer or any other person) in the home or otherwise than in a permanent retail establishment, and

"(B) the aggregate amount of the sales to such buyer during such calendar year is $5,000 or more,

then such person shall make a return, according to the forms or regulations prescribed by the Secretary, setting forth the name and address of the buyer to whom such sales are made.

"(2) DEFINITIONS.—For purposes of paragraph (1)—

"(A) BUY-SELL BASIS.—A transaction is on a buy-sell basis if the buyer performing the services is entitled to retain part or all of the difference between the price at which the buyer purchases the product and the price at which the buyer sells the product as part or all of the buyer's remuneration for the services, and

"(B) DEPOSIT-COMMISSION BASIS.—A transaction is on a deposit-commission basis if the buyer performing the services is entitled to retain part or all of a purchase deposit paid by the consumer in connection with the transaction as part or all of the buyer's remuneration for the services.

"(c) CERTAIN SERVICES NOT INCLUDED.—No return shall be required under subsection (a) or (b) if a statement with respect to the services is required to be furnished under section 6051, 6052, or 6053.

"(d) APPLICATIONS TO GOVERNMENTAL UNITS.—

"(1) TREATED AS PERSONS.—The term 'person' includes any governmental unit (and any agency or instrumentality thereof).

"(2) SPECIAL RULES.—In the case of any payment by a governmental entity or any agency or instrumentality thereof—

"(A) subsection (a) shall be applied without regard to the trade or business requirement contained therein, and

"(B) any return under this section shall be made by the officer or employee having control of the payment or appropriately designated for the purpose of making such return.

"(e) Statements To Be Furnished to Persons With Respect to Whom Information Is Required To Be Furnished.—Every person required to make a return under subsection (a) or (b) shall furnish to each person whose name is required to be set forth in such return a written statement showing—

"(1) the name and address of the person required to make such return, and

"(2) in the case of subsection (a), the aggregate amount of payments to the person required to be shown on such return.

The written statement required under the preceding sentence shall be furnished to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) was made.

"(f) Recipient To Furnish Name, Address, and Identification Number; Inclusion on Return.—

"(1) Furnishing of information.—Any person with respect to whom a return or statement is required under this section to be made by another person shall furnish to such other person his name, address, and identification number at such time and in such manner as the Secretary may prescribe by regulations.

"(2) Inclusion on return.—The person to whom an identification number is furnished under paragraph (1) shall include such number on any return which such person is required to file under this section and to which such identification number relates."

(b) Penalty for Failure to File Statement.—Section 6678(1) (relating to failure to file statement) is amended—

(1) by inserting "6041A(e)," after "6041(d),", and

(2) by inserting "6041A(a) or (b)," after "6041(a),".

(c) Effective Date.—The amendments made by this section shall apply to payments and sales made after December 31, 1982.

SEC. 313. STATE AND LOCAL INCOME TAX REFUNDS.

(a) In General.—Subpart B of part III of subchapter A of chapter 61 (relating to information concerning transactions with other persons) is amended by adding at the end thereof the following new section:

"SEC. 6050E. STATE AND LOCAL INCOME TAX REFUNDS.

"(a) Requirement of Reporting.—Every person who, with respect to any individual, during any calendar year makes payments of refunds of State or local income taxes (or allows credits or offsets with respect to such taxes) aggregating $10 or more shall make a return according to forms or regulations prescribed by the Secretary setting forth the aggregate amount of such payments, credits, or offsets, and the name and address of the individual with respect to whom such payment, credit, or offset was made.

"(b) Statements To Be Furnished to Individuals With Respect to Whom Information Is Furnished.—Every person making a return under subsection (a) shall furnish to each individual whose name is set forth in such return a written statement showing—

"(1) the name of the State or political subdivision thereof, and

"(2) the aggregate amount shown on the return of refunds, credits, and offsets to the individual.

The written statement required under the preceding sentence shall be furnished to the individual during January of the calendar year following the calendar year for which the return under subsection (a) was made.

"(c) Person Defined.—For purposes of this section, the term 'person' means the officer or employee having control of the payment of the refunds (or the allowance of the credits or offsets) or the person appropriately designated for purposes of this section."

(b) Conforming Amendment.—The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by adding at the end thereof the following new item:

"Sec. 6050E. State and local income tax refunds."

(c) Effective Date.—The amendments made by this section shall apply to payments of refunds, and credits and offsets made, after December 31, 1982.

SEC. 314. EMPLOYER REPORTING WITH RESPECT TO TIPS.

(a) In General.—Section 6053 (relating to reporting of tips) is amended by adding at the end thereof the following new subsection:

"(c) Reporting Requirements Relating to Certain Large Food or Beverage Establishments.—

"(1) Report to secretary.—In the case of a large food or beverage establishment, each employer shall report to the Secretary, at such time and manner as the Secretary may prescribe by regulation, the following information with respect to each calendar year:

"(A) The gross receipts of such establishment from the provision of food and beverages (other than nonallocable receipts).

"(B) The aggregate amount of charge receipts (other than nonallocable receipts).

"(C) The aggregate amount of charged tips shown on such charge receipts.

"(D) The sum of—

"(i) the aggregate amount reported by employees to the employer under subsection (a), plus

"(ii) the amount the employer is required to report under section 6041 with respect to service charges of less than 10 percent.

"(E) With respect to each employee, the amount allocated to such employee under paragraph (3).

"(2) Furnishing of statement to employees.—Each employer described in paragraph (1) shall furnish, in such manner as the Secretary may prescribe by regulations, to each employee of the large food or beverage establishment a written statement for each calendar year showing the following information:

"(A) The name and address of such employer.

"(B) The name of the employee.

"(C) The amount allocated to the employee under paragraph (3) for all payroll periods ending within the calendar year.

Any statement under this paragraph shall be furnished to the employee during January of the calendar year following the calendar year for which such statement is made.

"(3) EMPLOYEE ALLOCATION OF 8 PERCENT OF GROSS RECEIPTS.—

"(A) IN GENERAL.—For purposes of paragraphs (1)(E) and (2)(C), the employer of a large food or beverage establishment shall allocate (as tips for purposes of the requirements of this subsection) among employees performing services during any payroll period who customarily receive tip income an amount equal to the excess of—

"(i) 8 percent of the gross receipts (other than nonallocable receipts) of such establishment for the payroll period, over

"(ii) the aggregate amount reported by such employees to the employer under subsection (a) for such period.

"(B) METHOD OF ALLOCATION.—The employer shall allocate the amount under subparagraph (A)—

"(i) on the basis of a good faith agreement by the employer and the employees, or

"(ii) in the absence of an agreement under clause (i), in the manner determined under regulations prescribed by the Secretary.

"(C) THE SECRETARY MAY LOWER THE PERCENTAGE REQUIRED TO BE ALLOCATED.—The Secretary may reduce (but not below 5 percent) the percentage of gross receipts required to be allocated under subparagraph (A) where he determines that the percentage of gross receipts constituting tips is less than 8 percent.

"(4) LARGE FOOD OR BEVERAGE ESTABLISHMENT.—For purposes of this subsection, the term 'large food or beverage establishment' means any trade or business (or portion thereof)—

"(A) which provides food or beverages,

"(B) with respect to which the tipping of employees serving food or beverages by customers is customary, and

"(C) which normally employed more than 10 employees on a typical business day during the preceding calendar year.

For purposes of subparagraph (C), rules similar to the rules of subsections (a) and (b) of section 52 shall apply under regulations prescribed by the Secretary.

"(5) EMPLOYER NOT TO BE LIABLE FOR WRONG ALLOCATIONS.—The employer shall not be liable to any person if any amount is improperly allocated under paragraph (3)(A)(ii) if such allocation is done in accordance with the regulations prescribed under paragraph (3)(A)(ii).

"(6) NONALLOCABLE RECEIPTS DEFINED.—For purposes of this sebsection, the term 'nonallocable receipts' means receipts which are allocable to—

"(A) carryout sales, or

"(B) services with respect to which a service charge of 10 percent or more is added.

"(7) Application to new businesses.—The Secretary shall prescribe regulations for the application of this subsection to new businesses."

(b) Penalty for Failure To Furnish Statement.—Subparagraph (D) of section 6678(3) is amended by striking out "section 6053(b)" and inserting in lieu thereof "subsection (b) or (c) of section 6053(c)."

(c) Study of Tip Compliance.—The Secretary of the Treasury or his delegate shall submit before January 1, 1987, to the Committee on Ways and Means of the House of Representatives and to the Committee on Finance of the Senate a report with respect to tip compliance in the food and beverage service industry. Such study shall include, but not be limited to, an analysis of tipping patterns, tip-sharing arrangements, and tip compliance patterns.

(d) Conforming Amendment.—The last sentence of section 6001 (relating to notice or regulations requiring records, statements, and special returns) is amended by inserting ", records necessary to comply with section 6053(c)," after "charge receipts".

(e) Effective Dates.—

(1) In general. The amendments made by this section shall apply to calendar years beginning after December 31, 1982.

(2) Special rule for 1983. For purposes of section 60543(c) of the Internal Revenue Code of 1954, in the case of payroll periods ending before April 1, 1983, an employer must only report with respect to such periods—

(A) amounts described in subparagraphs (A), (B), (C), and (D) of section 6053(c)(1) of such Code, and

(B) the name, and identification number, wages paid to, and tips reported by, each tipped employee.

PART II—PROVISIONS TO IMPROVE REPORTING GENERALLY

SEC. 315. INCREASED PENALTIES FOR FAILURE TO FILE INFORMATION RETURN OR TO FURNISH STATEMENT.

(a) In General.—Subsection (a) of section 6652 (relating to failure to file certain information returns, etc.) is amended to read as follows:

"(a) Returns Relating to Information at Source, Payments of Dividends, Etc., and Certain Transfers of Stock.—

"(1) In general.—In the case of each failure—

"(A) to file a statement of the amount of payments to another person required by—

"(i) section 6041 (a) or (b) (relating to certain information at source),

"(ii) section 6042(a)(1) (relating to payments of dividends),

"(iii) section 6044(a)(1) (relating to payments of patronage dividends),

"(iv) section 6049(a) (relating to payments of interest),

"(v) section 6050A(a) (relating to reporting requirements of certain fishing boat operators), or

"(vi) section 6042(e), 6044(f), 6049(e), or 6051(d) (relating to information returns with respect to income tax withheld), or

"(B) to make a return required by—

"(i) subsection (a) or (b) of section 6041A (relating to returns of direct sellers),

"(ii) section 6045 (relating to returns of brokers),

"(iii) section 6052(a) (relating to reporting payment of wages in the form of group term life insurance), or

"(iv) section 6053(c)(1) (relating to reporting with respect to certain tips),

on the date prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not to willful neglect, there shall be paid (upon notice and demand by the Secretary and in the same manner as tax), by the person failing to file a statement referred to in subparagraph (A) or failing to make a return referred to in subparagraph (B), $50 for each such failure, but the total amount imposed on the delinquent person for all such failures during any calendar year shall not exceed $50,000.

"(2) PENALTY IN CASE OF INTENTIONAL DISREGARD.—If 1 or more failures to which paragraph (1) applies are due to intentional disregard of the filing requirement, then with respect to such failures—

"(A) the penalty imposed under paragraph (1) shall not be less than an amount equal to—

"(i) in the case of a return not described in clauses (ii) and (iii), 10 percent of the aggregate amount of the items required to be reported,

"(ii) in the case of a return required to be filed by section 6045, 5 percent of the gross proceeds required to be reported, and

"(iii) in the case of a return required to be filed by section 6041A(b), $100 for each such failure, and

"(B) the $50,000 limitation under paragraph (1) shall not apply."

(b) INCREASE IN ADDITION TO TAX FOR FAILURE TO FILE CERTAIN RETURNS OR STATEMENTS IN CONNECTION WITH PLANS OF DEFERRED COMPENSATION.—Subsection (f) of section 6652 (relating to information required in connection with certain plans of deferred compensation) is amended—

(1) by striking out "$10" and inserting in lieu thereof "$25", and

(2) by striking out "$5,000" and inserting in lieu thereof "$15,000".

(c) INCREASE IN CIVIL PENALTY FOR FAILURE TO FURNISH CERTAIN STATEMENTS.—Section 6678 (relating to failure to furnish certain statements) is amended—

(1) by striking out "$10" and inserting in lieu thereof "$50", and

(2) by striking out "$25,000" and inserting in lieu thereof "$50,000".

(d) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to returns or statements the due date for

the filing of which (without regard to extensions) is after December 31, 1982.

SEC. 316. INCREASE IN CIVIL PENALTY ON FAILURE TO SUPPLY IDENTIFYING NUMBERS.

(a) IN GENERAL.—Subsection (a) of section 6676 (relating to failure to supply identifying numbers) is amended to read as follows:

"(a) CIVIL PENALTIES.—

"(1) IN GENERAL.—If any person who is required by regulations prescribed under section 6109—

"(A) to include his taxpayer identification number in any return, statement, or other document,

"(B) to furnish his taxpayer identification number to another person, or

"(C) to include in any return, statement, or other document made with respect to another person the taxpayer identification number of such other person,

fails to comply with such requirement at the time prescribed by such regulations, such person shall, unless it is shown that such failure is due to reasonable cause and not to willful neglect, pay a penalty of $5 for each such failure described in subparagraph (A) and $50 for each such failure described in subparagraph (B) or (C), except that the total amount imposed on such person for all such failures during any calendar year shall not exceed $50,000.

"(2) TAXPAYER IDENTIFICATION NUMBER DEFINED.—The term 'taxpayer identification number' means the identifying number assigned to a person under section 6109."

(b) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to returns the due date for the filing of which (without regard to extensions) is after December 31, 1982.

SEC. 317. EXTENSION OF WITHHOLDING TO CERTAIN PAYMENTS WHERE IDENTIFYING NUMBER NOT FURNISHED OR INACCURATE.

(a) IN GENERAL.—Section 3402 (relating to withholding at source) is amended by adding at the end thereof the following new subsection:

"(s) EXTENSION OF WITHHOLDING TO CERTAIN PAYMENTS WHERE IDENTIFYING NUMBER NOT FURNISHED OR INACCURATE.—

"(1) IN GENERAL.—If, in the case of any backup withholding payment—

"(A) the payee fails to furnish his taxpayer identification number to the payor, or

"(B) the Secretary notifies the payor that the number furnished by the payee is incorrect,

then the payor shall deduct and withhold from such payment a tax equal to 15 percent of such payment.

"(2) PERIOD FOR WHICH WITHHOLDING IS IN EFFECT.—

"(A) FAILURE TO FURNISH NUMBER.—In the case of any failure described in subparagraph (A) of paragraph (1), paragraph (1) shall apply to any backup withholding payment made during the period during which the taxpayer identification number has not been furnished.

"(B) NOTIFICATION OF INCORRECT NUMBER.—In any case where there is a notification described in subparagraph (B)

of paragraph (1), paragraph (1) shall apply to any backup withholding payment made—

"(i) after the close of the 15th day after the day on which the payor was so notified, and

"(ii) before the payee furnishes another taxpayer identification number.

"(C) 15-DAY GRACE PERIODS.—

"(i) AFTER CORRECTION.—Unless the payor otherwise elects, paragraph (1) shall also apply to any backup withholding payment made after the close of the period described in subparagraph (A) or (B) (as the case may be) and before the 16th day after the close of such period.

"(ii) AFTER NOTIFICATION.—If the payor so elects, paragraph (1) shall also apply to any backup withholding payment made during the 15-day period described in clause (i) of subparagraph (B).

"(3) BACKUP WITHHOLDING PAYMENTS.—

"(A) IN GENERAL.—For purposes of this subsection, the term 'backup withholding payment' means any payment of a kind, and to a payee, required to be shown on a return required under—

"(i) section 6041 (a) or (b) (relating to certain information at source),

"(ii) section 6041A(a) (relating to returns regarding payments to nonemployees),

"(iii) section 6042(a) (relating to payments of dividends),

"(iv) section 6044 (relating to returns regarding patronage dividends) but only to the extent of payments of money,

"(v) section 6045 (relating to returns of brokers),

"(vi) section 6049(a) (relating to payments of interest), or

"(vii) section 6050A (relating to reporting requirements of certain fishing boat operators), but only to the extent of payments of the proceeds of the catch.

"(B) SPECIAL RULE.—For purposes of this subsection, the determination of whether any payment is of a kind required to be shown on a return described in subparagraph (A) shall be made without regard to any minimum amount which must be paid before a return is required.

"(4) PAYMENTS MUST AGGREGATE $600 BEFORE WITHHOLDING REQUIRED FROM PAYMENTS DESCRIBED IN SECTION 6041(a) OR 6041A.—In the case of any payment which is of a kind required to be shown on a return required under section 6041(a) or 6041A(a) and which is made during any calendar year, no amount shall be deducted and withheld with respect to such payment unless—

"(A) the aggregate amount of such payment and all previous such payments to the payee involved during such calendar year equals or exceeds $600,

"(B) the payor was required under section 6041(a) or 6041A(a) to file a return for the preceding calendar year with respect to payments to the payee involved, or

"(C) during the preceding calendar year the payor made backup withholding payments to the payee with respect to which amounts were required to be deducted and withheld under paragraph (1).

"(5) DEFINITIONS AND SPECIAL RULES.—For purposes of this subsection—

"(A) OBVIOUSLY INCORRECT NUMBER.—A payee shall be treated as failing to furnish his taxpayer identification number if the number furnished does not contain the proper number of digits.

"(B) PAYEE FURNISHES 2 INCORRECT NUMBERS.—If the payee furnishes a payor 2 incorrect numbers, the payor shall, after receiving notice of the second incorrect number, treat the payee as not having furnished another taxpayer identification number under paragraph (2)(B)(ii) until the day on which the payor receives notification from the Secretary that a correct taxpayer identification number has been furnished.

"(C) EXCEPTION FOR PAYMENTS TO CERTAIN PAYEES.—Paragraph (1) shall not apply to any payment made to—

"(i) the United States (as defined in section 3455(a)(3)),

"(ii) any State (as defined in section 3455(a)(2)),

"(iii) an organization which is exempt from taxation under section 501(a),

"(iv) any foreign government (as defined in section 3455(a)(4)) or international organization (as defined in section 3455(a)(5)), or

"(v) any other person specified in regulations.

"(D) TAXPAYER IDENTIFICATION NUMBER.—The term 'taxpayer identification number' means the identifying number assigned to a person under section 6109.

"(E) AMOUNTS FOR WHICH WITHHOLDING OTHERWISE REQUIRED.—No tax shall be deducted or withheld under this subsection with respect to any amount for which withholding is otherwise required by this title.

"(F) EXEMPTION WHILE WAITING FOR NUMBER.—The Secretary shall prescribe regulations for exemptions from the tax imposed by paragraph (1) during periods during which a person is waiting for receipt of a taxpayer identification number.

"(G) NOMINEES.—In the case of a backup withholding payment described in clause (i) or (v) of paragraph (3)(A) to a nominee, in the manner provided in regulations, both the nominee and the ultimate payee shall be treated as the payee.

"(H) REQUIREMENT OF NOTICE TO PAYEE.—Whenever the Secretary notifies a payor under paragraph (1)(B) that the taxpayer identification number furnished by any payee is incorrect, the Secretary shall at the same time furnish a

copy of such notice to the payor, and the payor shall promptly furnish such copy to the payee.

"(I) Requirement of notice to secretary.—If the Secretary notifies a payor under paragraph (1)(B) that the taxpayer identification number furnished by any payee is incorrect and such payee subsequently furnishes another taxpayer identification number to the payor, the payor shall promptly notify the Secretary of the other taxpayer identification number so furnished.

"(J) Coordination with other sections.—For purposes of section 31, this chapter (other than subsection (n) of this section), and so much of subtitle F (other than section 7205) as relates to this chapter, payments which are subject to withholding under this subsection shall be treated as if they were wages paid by an employer to an employee."

(b) Effective Date.—The amendments made by subsection (a) shall apply to payments made after December 31, 1983.

SEC. 318. MINIMUM PENALTY FOR EXTENDED FAILURE TO FILE.

(a) In General.—Subsection (a) of section 6651 (relating to failure to file tax return or to pay tax) is amended by adding at the end thereof the following new sentence:

"In the case of a failure to file a return of tax imposed by chapter 1 within 60 days of the date prescribed for filing of such return (determined with regard to any extensions of time for filing), unless it is shown that such failure is due to reasonable cause and not due to willful neglect, the addition to tax under paragraph (1) shall not be less than the lesser of $100 or 100 percent of the amount required to be shown as tax on such return."

(b) Conforming Amendments.—Section 6651(c)(1) (relating to additions under more than one paragraph) is amended—

(1) by adding at the end of subparagraph (A) the following new sentence: "In any case described in the last sentence of subsection (a), the amount of the addition under paragraph (1) of subsection (a) shall not be reduced under the preceding sentence below the amount provided in such last sentence.", and

(2) by inserting "(determined without regard to the last sentence of such subsection)" after "paragraph (1) of subsection (a)" in subparagraph (B).

(c) Effective Date.—The amendments made by this section shall apply to returns the due date for filing of which (including extensions) is after December 31, 1982.

SEC. 319. INFORMATION RETURNS.

Section 6011 (relating to general requirement of return, statement, or list) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) Regulations Requiring Returns on Magnetic Tape, Etc.—The Secretary shall prescribe regulations providing standards for determining which returns must be filed on magnetic media or in other machine-readable form. The Secretary may not require returns of any tax imposed by subtitle A on individuals, estates, and trusts to be other than on paper forms supplied by the Secretary. In prescribing such regulations, the Secretary shall take into account

(among other relevant factors) the ability of the taxpayer to comply at a reasonable cost with such a filing requirement."

Subtitle C—Abusive Tax Shelters, Etc.; Substantial Underpayments; False Documents; Frivolous Returns

PART I—ABUSIVE TAX SHELTERS, ETC.

SEC. 320. PENALTY FOR PROMOTING ABUSIVE TAX SHELTERS, ETC.

(a) GENERAL RULE.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding at the end thereof the following new section:

"SEC. 6700. PROMOTING ABUSIVE TAX SHELTERS, ETC.

"(a) IMPOSITION OF PENALTY.—Any person who—

"(1)(A) organizes (or assists in the organization of)—

"(i) a partnership or other entity,

"(ii) any investment plan or arrangement, or

"(iii) any other plan or arrangement, or

"(B) participates in the sale of any interest in an entity or plan or arrangement referred to in subparagraph (A), and

"(2) makes or furnishes (in connection with such organization or sale)—

"(A) a statement with respect to the allowability of any deduction or credit, the excludability of any income, or the securing of any other tax benefit by reason of holding an interest in the entity or participating in the plan or arrangement which the person knows or has reason to know is false or fraudulent as to any material matter, or

"(B) a gross valuation overstatement as to any material matter,

shall pay a penalty equal to the greater of $1,000 or 10 percent of the gross income derived or to be derived by such person from such activity.

"(b) RULES RELATING TO PENALTY FOR GROSS VALUATION OVERSTATEMENTS.—

"(1) GROSS VALUATION OVERSTATEMENT DEFINED.—For purposes of this section, the term 'gross valuation overstatement' means any statement as to the value of any property or services if—

"(A) the value so stated exceeds 200 percent of the amount determined to be the correct valuation, and

"(B) the value of such property or services is directly related to the amount of any deduction or credit allowable under chapter 1 to any participant.

"(2) AUTHORITY TO WAIVE.—The Secretary may waive all or any part of the penalty provided by subsection (a) with respect to any gross valuation overstatement on a showing that there was a reasonable basis for the valuation and that such valuation was made in good faith.

"(c) PENALTY IN ADDITION TO OTHER PENALTIES.—The penalty imposed by this section shall be in addition to any other penalty provided by law."

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 68 is amended by adding at the end thereof the following new item:

"Sec. 6700. Promoting abusive tax shelters, etc."

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the day after the date of the enactment of this Act.

SEC. 321. ACTION TO ENJOIN PROMOTERS OF ABUSIVE TAX SHELTERS, ETC.

(a) GENERAL RULE.—Subchapter A of chapter 76 (relating to civil actions by the United States) is amended by redesignating section 7408 as section 7409 and by inserting after section 7407 the following new section:

"SEC. 7408. ACTION TO ENJOIN PROMOTERS OF ABUSIVE TAX SHELTERS, ETC.

"(a) AUTHORITY TO SEEK INJUNCTION.—A civil action in the name of the United States to enjoin any person from further engaging in conduct subject to penalty under section 6700 (relating to penalty for promoting abusive tax shelters, etc.) may be commenced at the request of the Secretary. Any action under this section shall be brought in the district court of the United States for the district in which such person resides, has his principal place of business, or has engaged in conduct subject to penalty under section 6700. The court may exercise its jurisdiction over such action (as provided in section 7402(a)) separate and apart from any other action brought by the United States against such person.

"(b) ADJUDICATION AND DECREE.—In any action under subsection (a), if the court finds—

"(1) that the person has engaged in any conduct subject to penalty under section 6700 (relating to penalty for promoting abusive tax shelters, etc.), and

"(2) that injunctive relief is appropriate to prevent recurrence of such conduct,

the court may enjoin such person from engaging in such conduct or in any other activity subject to penalty under section 6700.

"(c) CITIZENS AND RESIDENTS OUTSIDE THE UNITED STATES.—If any citizen or resident of the United States does not reside in, and does not have his principal place of business in, any United States judicial district, such citizen or resident shall be treated for purposes of this section as residing in the District of Columbia."

(b) CLERICAL AMENDMENT.—The table of sections for subchapter A of chapter 76 is amended by striking out the last item and inserting in lieu thereof the following:

"Sec. 7408. Action to enjoin promoters of abusive tax shelters, etc.
"Sec. 7409. Cross references."

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the day after the date of the enactment of this Act.

SEC. 322. PROCEDURAL RULES APPLICABLE TO PENALTIES UNDER SECTIONS 6700, 6701, AND 6702.

(a) General Rule.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding at the end thereof the following new section:

"SEC. 6703. RULES APPLICABLE TO PENALTIES UNDER SECTIONS 6700, 6701, AND 6702.

"(a) Burden of Proof.—In any proceeding involving the issue of whether or not any person is liable for a penalty under section 6700, 6701, or 6702, the burden of proof with respect to such issue shall be on the Secretary.

"(b) Deficiency Procedures Not To Apply.—Subchapter B of chapter 63 (relating to deficiency procedures) shall not apply with respect to the assessment or collection of the penalties provided by sections 6700, 6701, and 6702.

"(c) Extension of Period of Collection Where Person Pays 15 Percent of Penalty.—

"(1) In general.—If, within 30 days after the day on which notice and demand of any penalty under section 6700, 6701, or 6702 is made against any person, such person pays an amount which is not less than 15 percent of the amount of such penalty and files a claim for refund of the amount so paid, no levy or proceeding in court for the collection of the remainder of such penalty shall be made, begun, or prosecuted until the final resolution of a proceeding begun as provided in paragraph (2). Notwithstanding the provisions of section 7421(a), the beginning of such proceeding or levy during the time such prohibition is in force may be enjoined by a proceeding in the proper court.

"(2) Person must bring suit in district court to determine his liability for penalty.—If, within 30 days after the day on which his claim for refund of any partial payment of any penalty under section 6700, 6701, or 6702 is denied (or, if earlier, within 30 days after the expiration of 6 months after the day on which he filed the claim for refund), the person fails to begin a proceeding in the appropriate United States district court for the determination of his liability for such penalty, paragraph (1) shall cease to apply with respect to such penalty, effective on the day following the close of the applicable 30-day period referred to in this paragraph.

"(3) Suspension of running of period of limitations on collection.—The running of the period of limitations provided in section 6502 on the collection by levy or by a proceeding in court in respect of any penalty described in paragraph (1) shall be suspended for the period during which the Secretary is prohibited from collecting by levy or a proceeding in court."

(b) Clerical Amendment.—The table of sections for subchapter B of chapter 68 is amended by adding at the end thereof the following new section:

"Sec. 6703. Rules applicable to penalties under sections 6700, 6701, and 6702."

(c) Effective Date.—The amendments made by this section shall take effect on the day after the date of the enactment of this Act.

PART II—SUBSTANTIAL UNDERPAYMENT; FALSE DOCUMENTS; FRIVOLOUS RETURNS; ETC.

SEC. 323. PENALTY FOR SUBSTANTIAL UNDERSTATEMENT.

(a) IN GENERAL.—Subchapter A of chapter 68 (relating to additions to tax and additional amounts) is amended by redesignating section 6661 as section 6662 and by inserting after section 6660 the following new section:

"SEC. 6661. SUBSTANTIAL UNDERSTATEMENT OF LIABILITY.

"(a) ADDITION TO TAX.—If there is a substantial understatement of income tax for any taxable year, there shall be added to the tax an amount equal to 10 percent of the amount of any underpayment attributable to such understatement.

"(b) DEFINITION AND SPECIAL RULE.—

"(1) SUBSTANTIAL UNDERSTATEMENT.—

"(A) IN GENERAL.—For purposes of this section, there is a substantial understatement of income tax for any taxable year if the amount of the understatement for the taxable year exceeds the greater of—

"(i) 10 percent of the tax required to be shown on the return for the taxable year, or

"(ii) $5,000.

"(B) SPECIAL RULE FOR CORPORATIONS.—In the case of a corporation other than an electing small business corporation (as defined in section 1371(b)) or a personal holding company (as defined in section 542), paragraph (1) shall be applied by substituting '$10,000' for '$5,000'.

"(2) UNDERSTATEMENT.—

"(A) IN GENERAL.—For purposes of paragraph (1), the term 'understatement' means the excess of—

"(i) the amount of the tax required to be shown on the return for the taxable year, over

"(ii) the amount of the tax imposed which is shown on the return.

"(B) REDUCTION FOR UNDERSTATEMENT DUE TO POSITION OF TAXPAYER OR DISCLOSED ITEM.—The amount of the understatement under subparagraph (A) shall be reduced by that portion of the understatement which is attributable to—

"(i) the tax treatment of any item by the taxpayer if there is or was substantial authority for such treatment, or

"(ii) any item with respect to which the relevant facts affecting the item's tax treatment are adequately disclosed in the return or in a statement attached to the return.

"(C) SPECIAL RULES IN CASES INVOLVING TAX SHELTERS.—

"(i) IN GENERAL.—In the case of any item attributable to a tax shelter—

"(I) subparagraph (B)(ii) shall not apply, and

"(II) subparagraph (B)(i) shall not apply unless (in addition to meeting the requirements of such subparagraph) the taxpayer reasonably believed

that the tax treatment of such item by the taxpayer was more likely than not the proper treatment.

"(ii) Tax shelter.—For purposes of clause (i), the term 'tax shelter' means—

"(I) a partnership or other entity,

"(II) any investment plan or arrangement, or

"(III) any other plan or arrangement,

if the principal purpose of such partnership, entity, plan, or arrangement is the avoidance or evasion of Federal income tax.

"(3) Coordination with penalty imposed by section 6659.—For purposes of determining the amount of the addition to tax assessed under subsection (a), there shall not be taken into account that portion of the substantial understatement on which a penalty is imposed under section 6659 (relating to addition to tax in the case of valuation overstatements).

"(c) Authority to Waive.—The Secretary may waive all or any part of the addition to tax provided by this section on a showing by the taxpayer that there was reasonable cause for the understatement (or part thereof) and that the taxpayer acted in good faith."

(b) Conforming Amendment.—The table of sections for subchapter A of chapter 68 is amended by striking out the last item and inserting in lieu thereof the following:

"Sec. 6661. Substantial understatement of liability.
"Sec. 6662. Applicable rules."

(c) Effective Date.—The amendments made by this section shall apply to returns the due date (determined without regard to extension) for filing of which is after December 31, 1982.

SEC. 324. PENALTIES FOR DOCUMENTS UNDERSTATING TAX LIABILITY.

(a) General Rule.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by inserting after section 6700 the following new section:

"SEC. 6701. PENALTIES FOR AIDING AND ABETTING UNDERSTATEMENT OF TAX LIABILITY.

"(a) Imposition of Penalty.—Any person—

"(1) who aids or assists in, procures, or advises with respect to, the preparation or presentation of any portion of a return, affidavit, claim, or other document in connection with any matter arising under the internal revenue laws,

"(2) who knows that such portion will be used in connection with any material matter arising under the internal revenue laws, and

"(3) who knows that such portion (if so used) will result in an understatement of the liability for tax of another person,

shall pay a penalty with respect to each such document in the amount determined under subsection (b).

"(b) Amount of Penalty.—

"(1) In general.—Except as provided in paragraph (2), the amount of the penalty imposed by subsection (a) shall be $1,000.

"(2) Corporations.—If the return, affidavit, claim, or other document relates to the tax liability of a corporation, the amount of the penalty imposed by subsection (a) shall be $10,000.

"(3) ONLY 1 PENALTY PER PERSON PER PERIOD.—If any person is subject to a penalty under subsection (a) with respect to any document relating to any taxpayer for any taxable period (or where there is no taxable period, any taxable event), such person shall not be subject to a penalty under subsection (a) with respect to any other document relating to such taxpayer for such taxable period (or event).

"(c) ACTIVITIES OF SUBORDINATES.—

"(1) IN GENERAL.—For purposes of subsection (a), the term 'procures' includes—

"(A) ordering (or otherwise causing) a subordinate to do an act, and

"(B) knowing of, and not attempting to prevent, participation by a subordinate in an act.

"(2) SUBORDINATE.—For purposes of paragraph (1), the term 'subordinate' means any other person (whether or not a director, officer, employee, or agent of the taxpayer involved) over whose activities the person has direction, supervision, or control.

"(d) TAXPAYER NOT REQUIRED TO HAVE KNOWLEDGE.—Subsection (a) shall apply whether or not the understatement is with the knowledge or consent of the persons authorized or required to present the return, affidavit, claim, or other document.

"(e) CERTAIN ACTIONS NOT TREATED AS AID OR ASSISTANCE.—For purposes of subsection (a)(1), a person furnishing typing, reproducing, or other mechanical assistance with respect to a document shall not be treated as having aided or assisted in the preparation of such document by reason of such assistance.

"(f) PENALTY IN ADDITION TO OTHER PENALTIES.—

"(1) IN GENERAL.—Except as provided by paragraph (2), the penalty imposed by this section shall be in addition to any other penalty provided by law.

"(2) COORDINATION WITH RETURN PREPARER PENALTIES.—No penalty shall be assessed under subsection (a) or (b) of section 6694 on any person with respect to any document for which a penalty is assessed on such person under subsection (a)."

(b) CLERICAL AMENDMENT.—The table of sections for subchapter B of chapter 68 is amended by inserting after the item relating to section 6700 the following new item:

"Sec. 6701. Penalties for aiding and abetting understatement of tax liability."

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the day after the date of the enactment of this Act.

(d) CROSS REFERENCE.—

For provisions relating to burden of proof and prepayment forum, see section 6703 of the Internal Revenue Code of 1954, as added by section 333 of this Act.

SEC. 325. FRAUD PENALTY.

(a) GENERAL RULE.—Subsection (b) of section 6653 (relating to fraud penalty) is amended to read as follows:

"(b) FRAUD.—

"(1) IN GENERAL.—If any part of any underpayment (as defined in subsection (c)) of tax required to be shown on a return

is due to fraud, there shall be added to the tax an amount equal to 50 percent of the underpayment.

"(2) Additional amount for portion attributable to fraud.—There shall be added to the tax (in addition to the amount determined under paragraph (1)) an amount equal to 50 percent of the interest payable under section 6601—

"(A) with respect to the portion of the underpayment described in paragraph (1) which is attributable to fraud, and

"(B) for the period beginning on the last day prescribed by law for payment of such underpayment (determined without regard to any extension) and ending on the date of the assessment of the tax (or, if earlier, the date of the payment of the tax).

"(3) No negligence addition when there is addition for fraud.—The addition to tax under this subsection shall be in lieu of any amount determined under subsection (a).

"(4) Special rule for joint returns.—In the case of a joint return under section 6013, this subsection shall not apply with respect to the tax of the spouse unless some part of the underpayment is due to the fraud of such spouse."

(b) Effective Date.—The amendment made by subsection (a) shall apply with respect to taxes the last day prescribed by law for payment of which (determined without regard to any extension) is after the date of enactment of this Act.

SEC. 326. PENALTY FOR FRIVOLOUS RETURNS.

(a) General Rule.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by inserting after section 6701 the following new section:

"SEC. 6702. FRIVOLOUS INCOME TAX RETURN.

"(a) Civil Penalty.—If—

"(1) any individual files what purports to be a return of the tax imposed by subtitle A but which—

"(A) does not contain information on which the substantial correctness of the self-assessment may be judged, or

"(B) contains information that on its face indicates that the self-assessment is substantially incorrect; and

"(2) the conduct referred to in paragraph (1) is due to—

"(A) a position which is frivolous, or

"(B) a desire (which appears on the purported return) to delay or impede the administration of Federal income tax laws,

then such individual shall pay a penalty of $500.

"(b) Penalty in Addition to Other Penalties.—The penalty imposed by subsection (a) shall be in addition to any other penalty provided by law."

(b) Clerical Amendment.—The table of sections for subchapter B of chapter 68 is amended by inserting after the item relating to section 6701 the following new item:

"Sec. 6702. Frivolous income tax return."

(c) Effective Date.—The amendments made by this section shall apply with respect to documents filed after the date of the enactment of this Act.

(d) Cross Reference.—

For provisions relating to burden of proof and prepayment forum, see section 6703 of the Internal Revenue Code of 1954, as added by section 333 of this Act.

SEC. 327. RELIEF FROM CRIMINAL PENALTY FOR FAILURE TO FILE ESTIMATED TAX WHERE TAXPAYER FALLS WITHIN STATUTORY EXCEPTIONS.

Section 7203 (relating to willful failure to file return, supply information, or pay tax) is amended by adding at the end thereof the following new sentence: "In the case of any person with respect to whom there is a failure to pay any estimated tax, this section shall not apply to such person with respect to such failure if there is no addition to tax under section 6654 or 6655 with respect to such failure."

SEC. 328. ADJUSTMENTS TO ESTIMATED TAX PROVISIONS.

(a) Waiver of Penalty Where Individual Did Not Have Tax Liabilities for Preceding Taxable Year.—

(1) Section 6654 (relating to failure by individual to pay estimated tax) is amended by redesignating subsection (h) as subsection (i) and by inserting after subsection (g) the following new subsection:

"(h) Exception Where No Tax Liability for Preceding Taxable Year.—No addition to tax shall be imposed under subsection (a) for any taxable year if—

"(1) the individual did not have any liability for tax for the preceding taxable year,

"(2) the preceding taxable year was a taxable year of 12 months, and

"(3) the individual was a citizen or resident of the United States throughout the preceding taxable year."

(2) Subsection (g) of section 6654 is amended by striking out "and (f)" and inserting in lieu thereof "(f), and (h)".

(b) Elimination of Requirements To File Declarations of Estimated tax.—

(1) Section 6015 (relating to declaration of estimated income tax by individuals) is amended by adding at the end thereof the following new subsection:

"(k) Termination.—No declaration shall be required under this section for any taxable year beginning after December 31, 1982."

(2) Section 6073 (relating to time for filing declarations of estimated income tax by individuals) is amended by adding at the end thereof the following new subsection:

"(f) Termination.—This section shall not apply to any taxable year beginning after December 31, 1982."

(3) Section 6153 (relating to installment payments of estimated income tax by individuals) is amended by striking out subsection (g) and inserting in lieu thereof the following:

"(g) Special Rules for Taxable Years Beginning After 1982.—In the case of taxable years beginning after 1982—

"(1) this section shall be applied as if the requirements of sections 6015 and 6073 remained in effect, and

"(2) the amount of the estimated tax taken into account under this section shall be determined under rules similar to the rules of subsections (b) and (d) of section 6654."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1982.

SEC. 329. INCREASES IN CERTAIN CRIMINAL FINES.

(a) ATTEMPT TO EVADE OR DEFEAT TAX.—Section 7201 (relating to attempt to evade or defeat tax) is amended by striking out "$10,000" and inserting in lieu thereof "$100,000 ($500,000 in the case of a corporation)".

(b) WILLFUL FAILURE TO FILE RETURN, SUPPLY INFORMATION, OR PAY TAX.—Section 7203 (relating to willful failure to file return, supply information, or pay tax) is amended by striking out "$10,000" and inserting in lieu thereof "$25,000 ($100,000 in the case of a corporation)".

(c) FRAUD AND FALSE STATEMENTS.—Section 7206 (relating to fraud and false statements) is amended by striking out "$5,000" and inserting in lieu thereof "$100,000 ($500,000 in the case of a corporation)".

(d) FRAUDULENT RETURNS, STATEMENTS, OR OTHER DOCUMENTS.—Section 7207 (relating to fraudulent returns, statements, or other documents) is amended by striking out "$1,000" each place it appears and inserting in lieu thereof "$10,000 ($50,000 in the case of a corporation)".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to offenses committed after the date of the enactment of this Act.

SEC. 330. SPECIAL RULES WITH RESPECT TO CERTAIN CASH.

(a) IN GENERAL.—Subchapter A of chapter 70 (relating to jeopardy) is amended by adding at the end thereof the following new part:

"PART III—SPECIAL RULES WITH RESPECT TO CERTAIN CASH

"Sec. 6867. Presumptions where owner of large amount of cash is not identified.

"SEC. 6867. PRESUMPTIONS WHERE OWNER OF LARGE AMOUNT OF CASH IS NOT IDENTIFIED.

"(a) GENERAL RULE.—If the individual who is in physical possession of cash in excess of $10,000 does not claim such cash—

"(1) as his, or

"(2) as belonging to another person whose identity the Secretary can readily ascertain and who acknowledges ownership of such cash,

then, for purposes of sections 6851 and 6861, it shall be presumed that such cash represents gross income of a single individual for the taxable year in which the possession occurs, and that the collection of tax will be jeopardized by delay.

"(b) RULES FOR ASSESSING.—In the case of any assessment resulting from the application of subsection (a)—

"(1) the entire amount of the cash shall be treated as taxable income for the taxable year in which the possession occurs,

"(2) such income shall be treated as taxable at a 50-percent rate, and

"(3) except as provided in subsection (c), the possessor of the cash shall be treated (solely with respect to such cash) as the taxpayer for purposes of chapters 63 and 64 and section 7429(a)(1).

"(c) EFFECT OF LATER SUBSTITUTION OF TRUE OWNER.—If, after an assessment resulting from the application of subsection (a), such assessment is abated and replaced by an assessment against the owner of the cash, such later assessment shall be treated for purposes of all laws relating to lien, levy and collection as relating back to the date of the original assessment.

"(d) DEFINITIONS.—For purposes of this section—

"(1) CASH.—The term 'cash' includes any cash equivalent.

"(2) CASH EQUIVALENT.—The term 'cash equivalent' means—

"(A) foreign currency,

"(B) any bearer obligation, and

"(C) any medium of exchange which—

"(i) is of a type which has been frequently used in illegal activities, and

"(ii) is specified as a cash equivalent for purposes of this part in regulations prescribed by the Secretary.

"(3) VALUE OF CASH EQUIVALENT.—Any cash equivalent shall be taken into account—

"(A) in the case of a bearer obligation, at its face amount, and

"(B) in the case of any other cash equivalent, at its fair market value."

(b) CLERICAL AMENDMENT.—The table of parts for such subchapter A is amended by adding at the end thereof the following new item:

"Part III. Special rules with respect to certain cash."

(c) EFFECTIVE DATE.—The amendments made by subsections (a) and (b) shall take effect on the day after the date of the enactment of this Act.

Subtitle D—Administrative Summons

SEC. 331. SPECIAL PROCEDURES FOR THIRD-PARTY SUMMONSES.

(a) PROCEEDING TO QUASH.—Paragraph (2) of section 7609(b) (relating to right to intervene; right to stay compliance) is amended to read as follows:

"(2) PROCEEDING TO QUASH.—

"(A) IN GENERAL.—Notwithstanding any other law or rule of law, any person who is entitled to notice of a summons under subsection (a) shall have the right to begin a proceeding to quash such summons not later than the 20th day after the day such notice is given in the manner provided in subsection (a)(2). In any such proceeding, the Secretary may seek to compel compliance with the summons.

"(B) REQUIREMENT OF NOTICE TO PERSON SUMMONED AND TO SECRETARY.—If any person begins a proceeding under

subparagraph (A) with respect to any summons, not later than the close of the 20-day period referred to in subparagraph (A) such person shall mail by registered or certified mail a copy of the petition to the person summoned and to such office as the Secretary may direct in the notice referred to in subsection (a)(1).

"(C) Intervention; etc.—Notwithstanding any other law or rule of law, the person summoned shall have the right to intervene in any proceeding under subparagraph (A). Such person shall be bound by the decision in such proceeding (whether or not the person intervenes in such proceeding)."

(b) Restriction on Examination.—Subsection (d) of section 7609 (relating to restriction on examination of records) is amended to read as follows:

"(d) Restriction on Examination of Records.—No examination of any records required to be produced under a summons as to which notice is required under subsection (a) may be made—

"(1) before the close of the 23rd day after the day notice with respect to the summons is given in the manner provided in subsection (a)(2), or

"(2) where a proceeding under subsection (b)(2)(A) was begun within the 20-day period referred to in such subsection and the requirements of subsection (b)(2)(B) have been met, except in accordance with an order of the court having jurisdiction of such proceeding or with the consent of the person beginning the proceeding to quash."

(c) Jurisdiction.—Subsection (h) of section 7609 (relating to jurisdiction of district court) is amended to read as follows:

"(h) Jurisdiction of District Court; Etc.—

"(1) Jurisdiction.—The United States district court for the district within which the person to be summoned resides or is found shall have jurisdiction to hear and determine any proceeding brought under subsection (b)(2), (f), or (g). An order denying the petition shall be deemed a final order which may be appealed.

"(2) Special rule for proceedings under subsections (f) and (g).—The determinations required to be made under subsections (f) and (g) shall be made ex parte and shall be made solely on the petition and supporting affidavits.

"(3) Priority.—Except as to cases the court considers of greater importance, a proceeding brought for the enforcement of any summons, or a proceeding under this section, and appeals, takes precedence on the docket over all other cases and shall be assigned for hearing and decided at the earliest practicable date."

(d) Conforming Amendments.—

(1) Paragraph (1) of section 7609(a) is amended—

(A) by striking out "14th day" and inserting in lieu thereof "23rd day", and

(B) by striking out the last sentence and inserting in lieu thereof the following: "Such notice shall be accompanied by a copy of the summons which has been served and shall

contain an explanation of the right under subsection (b)(2) to bring a proceeding to quash the summons."

(2) The subsection heading for subsection (b) of section 7609 is amended to read as follows:

"(b) RIGHT TO INTERVENE; RIGHT TO PROCEEDING TO QUASH.—".

(e) EFFECTIVE DATE.—The amendments made by this section shall apply to summonses served after December 31, 1982.

SEC. 332. DUTY OF THIRD-PARTY RECORDKEEPER.

(a) GENERAL RULE.—Section 7609 (relating to special procedures for third-party summonses) is amended by adding at the end thereof the following new subsection:

"(i) DUTY OF THIRD-PARTY RECORDKEEPER.—

"(1) RECORDKEEPER MUST ASSEMBLE RECORDS AND BE PREPARED TO PRODUCE RECORDS.—On receipt of a summons described in subsection (c), the third-party recordkeeper shall proceed to assemble the records requested, or such portion thereof as the Secretary may prescribe, and shall be prepared to produce the records pursuant to the summons on the day on which the records are to be examined.

"(2) SECRETARY MAY GIVE RECORDKEEPER CERTIFICATE.—The Secretary may issue a certificate to the third-party recordkeeper that the period prescribed for beginning a proceeding to quash a summons has expired and that no such proceeding began within such period, or that the taxpayer consents to the examination.

"(3) PROTECTION FOR RECORDKEEPER WHO DISCLOSES.—Any third-party recordkeeper, or agent or employee thereof, making a disclosure of records pursuant to this section in good-faith reliance on the certificate of the Secrtetary or an order of a court requiring production of records shall not be liable to any customer or other person for such disclosure."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to summonses served after December 31, 1982.

SEC. 333. LIMITATION ON USE OF ADMINISTRATIVE SUMMONS.

(a) IN GENERAL.—Section 7602 (relating to examination of books and witnesses) is amended by striking out "For the purpose" and inserting in lieu thereof "(a) AUTHORITY TO SUMMON, ETC.—For the purpose" and by adding at the end thereof the following new subsections:

"(b) PURPOSE MAY INCLUDE INQUIRY INTO OFFENSE.—The purposes for which the Secretary may take any action described in paragraph (1), (2), or (3) of subsection (a) include the purpose of inquiring into any offense connected with the administration or enforcement of the internal revenue laws.

"(c) NO ADMINISTRATIVE SUMMONS WHEN THERE IS JUSTICE DEPARTMENT REFERRAL.—

"(1) LIMITATION OF AUTHORITY.—No summons may be issued under this title, and the Secretary may not begin any action under section 7604 to enforce any summons, with respect to any person if a Justice Department referral is in effect with respect to such person.

"(2) JUSTICE DEPARTMENT REFERRAL IN EFFECT.—For purposes of this subsection—

"(A) In general.—A Justice Department referral is in effect with respect to any person if—

"(i) the Secretary has recommended to the Attorney General a grand jury investigation of, or the criminal prosecution of, such person for any offense connected with the administration or enforcement of the internal revenue laws, or

"(ii) any request is made under section 6103(h)(3)(B) for the disclosure of any return or return information (within the meaning of section 6103(b)) relating to such person.

"(B) Termination.—A Justice Department referral shall cease to be in effect with respect to a person when—

"(i) the Attorney General notifies the Secretary, in writing, that—

"(I) he will not prosecute such person for any offense connected with the administration or enforcement of the internal revenue laws,

"(II) he will not authorize a grand jury investigation of such person with respect to such an offense, or

"(III) he will discontinue such a grand jury investigation,

"(ii) a final disposition has been made of any criminal proceeding pertaining to the enforcement of the internal revenue laws which was instituted by the Attorney General against such person, or

"(iii) the Attorney General notifies the Secretary, in writing, that he will not prosecute such person for any offense connected with the administration or enforcement of the internal revenue laws relating to the request described in subparagraph (A)(ii).

"(3) Taxable years, etc., treated separately.—For purposes of this subsection, each taxable period (or, if there is no taxable period, each taxable event) and each tax imposed by a separate chapter of this title shall be treated separately."

(b) Effective Date.—The amendments made by subsection (a) shall take effect on the day after the date of the enactment of this Act.

Subtitle E—Withholding on Pensions and Other Retirement Income

SEC. 334. WITHHOLDING ON PENSIONS, ANNUITIES, AND CERTAIN OTHER DEFERRED INCOME.

(a) In General.—Chapter 24 (relating to collection of income tax at source on wages) is amended by adding at the end thereof the following new section:

"SEC. 3405. SPECIAL RULES FOR PENSIONS, ANNUITIES, AND CERTAIN OTHER DEFERRED INCOME.

"(a) Pensions, Annuities, Etc.—

"(1) Withholding as if payment were wages.—The payor of any periodic payment (as defined in subsection (d)(2)) shall withhold from such payment the amount which would be required to be withheld from such payment if such payment were a payment of wages by an employer to an employee for the appropriate payroll period.

"(2) Election of no withholding.—An individual may elect to have paragraph (1) not apply with respect to periodic payments made to such individual. Such an election shall remain in effect until revoked by such individual.

"(3) When election takes effect.—Any election under this subsection (and any revocation of such an election) shall take effect as provided by subsection (f)(3) of section 3402 for withholding exemption certificates.

"(4) Amount withheld where no withholding exemption certificate in effect.—In the case of any payment with respect to which a withholding exemption certificate is not in effect, the amount withheld under paragraph (1) shall be determined by treating the payee as a married individual claiming 3 withholding exemptions.

"(b) Nonperiodic Distribution.—

"(1) Withholding.—The payor of any nonperiodic distribution (as defined in subsection (d)(3)) shall withhold from such distribution the amount determined under paragraph (2).

"(2) Amount of withholding.—

"(A) Distributions which are not qualified total distributions.—In the case of any nonperiodic distribution which is not a qualified total distribution, the amount withheld under paragraph (1) shall be the amount determined by multiplying such distribution by 10 percent.

"(B) Qualified total distributions.—In the case of any nonperiodic distribution which is a qualified total distribution, the amount withheld under paragraph (1) shall be determined under tables (or other computational procedures) prescribed by the Secretary which are based on the amount of tax which would be imposed on such distribution under section 402(e) if the recipient elected to treat such distribution as a lump-sum distribution (within the meaning of section 402(e)(4)(A)).

"(C) Special rule for distributions by reasons of death.—In the case of any distribution described in subparagraph (B) from or under any plan or contract described in section 401(a), 403(a), or 403(b) which is made by reason of a participant's death, the Secretary, in prescribing tables or procedures under paragraph (1), shall take into account the exclusion from gross income provided by section 101(b) (whether or not allowable).

"(3) Election of no withholding.—

"(A) In general.—An individual may elect not to have paragraph (1) apply with respect to any nonperiodic distribution.

"(B) Scope of election.—An election under subparagraph (A)—

"(i) except as provided in clause (ii), shall be on a distribution-by-distribution basis, or

"(ii) to the extent provided in regulations, may apply to subsequent nonperiodic distributions made by the payor to the payee under the same arrangement.

"(c) Liability for Withholding.—

"(1) In general.—Except as provided in paragraph (2), the payor of a designated distribution (as defined in subsection (d)(1)) shall withhold, and be liable for, payment of the tax required to be withheld under this section.

"(2) Plan administrator liable in certain cases.—

"(A) In general.—In the case of any plan to which this paragraph applies, paragraph (1) shall not apply and the plan administrator shall withhold, and be liable for, payment of the tax unless the plan administrator—

"(i) directs the payor to withhold such tax, and

"(ii) provides the payor with such information as the Secretary may require by regulations.

"(B) Plans to which paragraph applies.—This paragraph applies to any plan described in, or which at any time has been determined to be described in—

"(i) section 401(a),

"(ii) section 403(a), or

"(iii) section 301(d) of the Tax Reduction Act of 1975.

"(d) Definitions and Special Rules.—For purposes of this section—

"(1) Designated distribution.—

"(A) In general.—Except as provided in subparagraph (B), the term 'designated distribution' means any distribution or payment from or under—

"(i) an employer deferred compensation plan,

"(ii) an individual retirement plan (as defined in section 7701(a)(37)), or

"(iii) a commercial annuity.

"(B) Exceptions.—The term 'designated distribution' shall not include—

"(i) any amount which is wages without regard to this section, and

"(ii) the portion of a distribution or payment which it is reasonable to believe is not includible in gross income.

"(2) Periodic payment.—The term 'periodic payment' means a designated distribution which is an annuity or similar periodic payment.

"(3) Nonperiodic distribution.—The term 'nonperiodic distribution' means any designated distribution which is not a periodic payment.

"(4) Qualified total distribution.—

"(A) In general.—The term 'qualified total distribution' means any distribution which—

"(i) is a designated distribution,

"(ii) it is reasonable to believe is made within 1 taxable year of the recipient,

"(iii) is made under a plan described in section 401(a), or 403(a), and

"(iv) consists of the balance to the credit of the employee under such plan.

"(B) Special rule for accumulated deductible employee contributions.—For purposes of subparagraph (A), accumulated deductible employee contributions (within the meaning of section 72(o)(5)(B)) shall be treated separately in determining if there has been a qualified total distribution.

"(5) Employer deferred compensation plan.—The term 'employer deferred compensation plan' means any pension, annuity, profit-sharing, or stock bonus plan or other plan deferring the receipt of compensation.

"(6) Commercial annuity.—The term 'commercial annuity' means an annuity, endowment, or life insurance contract issued by an insurance company licensed to do business under the laws of any State.

"(7) Plan administrator.—The term 'plan administrator' has the meaning given such term by section 414(g).

"(8) Maximum amount withheld.—The maximum amount to be withheld under this section on any designated distribution shall not exceed the sum of the amount of money and the fair market value of other property (other than employer securities of the employer corporation (within the meaning of section 402(a)(3))) received in the distribution.

"(9) Separate arrangements to be treated separately.—If the payor has more than 1 arrangement under which designated distributions may be made to any individual, each such arrangement shall be treated separately.

"(10) Time and manner of election.—

"(A) In general.—Any election and any revocation under this section shall be made at such time and in such manner as the Secretary shall prescribe.

"(B) Payor required to notify payee of rights to elect.—

"(i) Periodic payments.—The payor of any periodic payment—

"(I) shall transmit to the payee notice of the right to make an election under subsection (a) not earlier than 6 months before the first of such payments and not later than when making the first of such payments,

"(II) is such a notice is not transmitted under subclause (I) when making such first payment, shall transmit such a notice when making such first payment, and

"(III) shall transmit to payees, not less frequently than once each calendar year, notice of their rights to make elections under subsection (a) and to revoke such elections.

"(ii) Nonperiodic distributions.—The payor of any nonperiodic distribution shall transmit to the payee notice of the right to make any election provided in

subsection (b) at the time of the distribution (or at such earlier time as may be provided in regulations).

"(iii) NOTICE.—Any notice transmitted pursuant to this subparagraph shall be in such form and contain such information as the Secretary shall prescribe.

"(11) WITHHOLDING INCLUDES DEDUCTION.—The terms 'withholding', 'withhold', and 'withheld' include 'deducting', 'deduct', and 'deducted'.

"(e) WITHHOLDING TO BE TREATED AS WAGE WITHHOLDING UNDER SECTION 3402 FOR OTHER PURPOSES.—For purposes of this chapter (and so much of subtitle F as relates to this chapter)—

"(1) any designated distribution (whether or not an election under this section applies to such distribution) shall be treated as if it were wages paid by an employer to an employee with respect to which there has been withholding under section 3402, and

"(2) in the case of any designated distribution not subject to withholding under this section by reason of an election under this section, the amount withheld shall be treated as zero."

(b) FILING OF REPORTS.—Section 6047 (relating to information concerning certain trusts and annuity and bond purchase plans) is amended by redesignating subsection (e) as subsection (f) and by inserting after subsection (d) the following new subsection:

"(e) REPORTS BY EMPLOYERS, PLAN ADMINISTRATORS, ETC.—

"(1) IN GENERAL.—The Secretary shall by forms or regulations require that—

"(A) the employer maintaining, or the plan administrator (within the meaning of section 414(g)) of, a plan from which designated distributions (as defined in section 3405(d)(1)) may be made, and

"(B) any person issuing any contract under which designated distributions (as so defined) may be made,

make returns and reports regarding such plan (or contract) to the Secretary, to the participants and beneficiaries of such plan (or contract), and to such other persons as the Secretary may by regulations prescribe.

"(2) FORM, ETC., OF REPORTS.—Such reports shall be in such form, made at such time, and contain such information as the Secretary may prescribe by forms or regulations."

(c) PENALTY FOR FAILURE TO KEEP RECORDS NECESSARY TO COMPLY WITH REPORTING REQUIREMENTS OF SECTION 6047(e).—

(1) IN GENERAL.—Subchapter B of chapter 68 (relating to assessable penalties) is amended by adding at the end thereof the following new section:

"SEC. 6704. FAILURE TO KEEP RECORDS NECESSARY TO MEET REPORTING REQUIREMENTS UNDER SECTION 6047(e).

"(a) LIABILITY FOR PENALTY.—Any person who—

"(1) has a duty to report or may have a duty to report any information under section 6047(e), and

"(2) fails to keep such records as may be required by regulations prescribed under section 6047(e) for the purpose of providing the necessary data base for either current reporting or future reporting,

shall pay a penalty for each calendar year for which there is any failure to keep such records.

"*(b)* AMOUNT OF PENALTY.—

"*(1)* IN GENERAL.—*The penalty of any person for any calendar year shall be $50, multiplied by the number of individuals with respect to whom such failure occurs in such year.*

"*(2)* MAXIMUM AMOUNT.—*The penalty under this section of any person for any calendar year shall not exceed $50,000.*

"*(c)* EXCEPTIONS.—

"*(1)* REASONABLE CAUSE.—*No penalty shall be imposed by this section on any person for any failure which is shown to be due to reasonable cause and not to willful neglect.*

"*(2)* INABILITY TO CORRECT PREVIOUS FAILURE.—*No penalty shall be imposed by this section on any failure by a person if such failure is attributable to a prior failure which has been penalized under this section and with respect to which the person has made all reasonable efforts to correct the failure.*

"*(3)* PRE-1983 FAILURES.—*No penalty shall be imposed by this section on any person for any failure which is attributable to a failure occurring before January 1, 1983, if the person has made all reasonable efforts to correct such pre-1983 failure.*"

(2) CLERICAL AMENDMENT.—*The table of sections for subchapter B of chapter 68 is amended by adding at the end thereof the following new section:*

"*Sec. 6704. Failure to keep records necessary to meet reporting requirements under section 6047(e).*"

(d) COORDINATION WITH VOLUNTARY WITHHOLDING ON CERTAIN PAYMENTS OTHER THAN WAGES.—*Subsection (o) of section 3402 (relating to extension of withholding to certain payments other than wages) is amended by adding at the end thereof the following new paragraph:*

"*(6)* COORDINATION WITH WITHHOLDING ON DESIGNATED DISTRIBUTIONS UNDER SECTION 3405.—*This subsection shall not apply to any amount which is a designated distribution (within the meaning of section 3405(d)(1)).*"

(e) EFFECTIVE DATES.—

(1) AMENDMENT MADE BY SUBSECTIONS *(a)* AND *(d)*.—*Except as provided in paragraph (4), the amendment made by subsections (a) and (d) shall apply to payments or other distributions made after December 31, 1982.*

(2) AMENDMENTS MADE BY SUBSECTION *(b)*.—*Except as provided in paragraph (4), the amendments made by subsection (b) shall take effect on January 1, 1983.*

(3) AMENDMENTS MADE BY SUBSECTION *(c)*.—*The amendments made by subsection (c) shall take effect on January 1, 1985.*

(4) PERIODIC PAYMENTS BEGINNING BEFORE JANUARY 1, 1983.—*For purposes of section 3405(a) of the Internal Revenue Code of 1954, in the case of periodic payments beginning before January 1, 1983, the first periodic payment after December 31, 1982, shall be treated as the first such periodic payment.*

(5) DELAY IN APPLICATION.—*The Secretary of the Treasury shall prescribe such regulations which delay (but not beyond June 30, 1983) the application of some or all of the amendments*

made by this section with respect to any payor until such time as such payor is able to comply without undue hardship with the requirements of such provisions.

(6) Waiver of penalty.—No penalty shall be assessed under section 6672 with respect to any failure to withhold as required by the amendments made by this section if such failure was before July 1, 1983, and if the person made a good faith effort to comply with such withholding requirements.

SEC. 335. PARTIAL ROLLOVERS OF IRA DISTRIBUTIONS PERMITTED.

(a) General Rule.—

(1) Paragraph (3) of section 408(d) is amended by adding at the end thereof the following new subparagraph:

"(C) Partial rollovers permitted.—

"(i) In general.—If any amount paid or distributed out of an individual retirement account or individual retirement annuity would meet the requirements of subparagraph (A) but for the fact that the entire amount was not paid into an eligible plan as required by clause (i), (ii), or (iii) of subparagraph (A), such amount shall be treated as meeting the requirements of subparagraph (A) to the extent it is paid into an eligible plan referred to in such clause not later than the 60th day referred to in such clause.

"(ii) Eligible plan.—For purposes of clause (i), the term 'eligible plan' means any account, annuity, bond, contract, or plan referred to in subparagraph (A)."

(2) Paragraph (3) of section 409(b) is amended by adding at the end thereof the following new subparagraph:

"(D) Partial rollovers permitted.—Rules similar to the rules of section 408(d)(3)(C) shall apply for purposes of subparagraph (C)."

(b) Effective Date.—The amendments made by subsection (a) shall apply to distributions made after December 31, 1982, in taxable years ending after such date.

Subtitle F—Transactions Outside the United States or Involving Foreign Persons

SEC. 336. JURISDICTION OF COURT AND ENFORCEMENT OF SUMMONS IN CASE OF PERSONS RESIDING OUTSIDE THE UNITED STATES.

(a) General Rule.—Subsection (a) of section 7701 (relating to definitions) is amended by adding at the end thereof the following new paragraph:

"(38) Persons residing outside United States.—If any citizen or resident of the United States does not reside in (and is not found in) any United States judicial district, such citizen or resident shall be treated as residing in the District of Columbia for purposes of any provision of this title relating to—

"(A) jurisdiction of courts, or

"(B) enforcement of summons."

(b) Effective Date.—The amendment made by subsection (a) shall take effect on the day after the date of the enactment of this Act.

SEC. 337. ADMISSIBILITY OF EVIDENCE MAINTAINED IN FOREIGN COUNTRIES.

(a) General Rule.—Part III of subchapter N of chapter 1 (relating to income from sources without the United States) is amended by adding at the end thereof the following new subpart:

"Subpart I—Admissibility of Documentation Maintained in Foreign Countries

"Sec. 982. Admissibility of documentation maintained in foreign countries.

"SEC. 982. ADMISSIBILITY OF DOCUMENTATION MAINTAINED IN FOREIGN COUNTRIES.

"(a) General Rule.—If the taxpayer fails to substantially comply with any formal document request arising out of the examination of the tax treatment of any item (hereinafter in this section referred to as the 'examined item') before the 90th day after the date of the mailing of such request on motion by the Secretary, any court having jurisdiction of a civil proceeding in which the tax treatment of the examined item is an issue shall prohibit the introduction by the taxpayer of any foreign-based documentation covered by such request.

"(b) Reasonable Cause Exception.—

"(1) In general.—Subsection (a) shall not apply with respect to any documentation if the taxpayer establishes that the failure to provide the documentation as requested by the Secretary is due to reasonable cause.

"(2) Foreign nondisclosure law not reasonable cause.—For purposes of paragraph (1), the fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the requested documentation is not reasonable cause.

"(c) Formal Document Request.—For purposes of this section—

"(1) Formal document request.—The term 'formal document request' means any request (made after the normal request procedures have failed to produce the requested documentation) for the production of foreign-based documentation which is mailed by registered or certified mail to the taxpayer at his last known address and which sets forth—

"(A) the time and place for the production of the documentation,

"(B) a statement of the reason the documentation previously produced (if any) is not sufficient,

"(C) a description of the documentation being sought, and

"(D) the consequences to the taxpayer of the failure to produce the documentation described in subparagraph (C).

"(2) Proceeding to quash.—

"(A) In general.—Notwithstanding any other law or rule of law, any person to whom a formal document request

is mailed shall have the right to begin a proceeding to quash such request not later than the 90th day after the day such request was mailed. In any such proceeding, the Secretary may seek to compel compliance with such request.

"(B) JURISDICTION.—The United States district court for the district in which the person (to whom the formal document request is mailed) resides or is found shall have jurisdiction to hear any proceeding brought under subparagraph (A). An order denying the petition shall be deemed a final order which may be appealed.

"(C) SUSPENSION OF 90-DAY PERIOD.—The running of the 90-day period referred to in subsection (a) shall be suspended during any period during which a proceeding brought under subparagraph (A) is pending.

"(d) DEFINITIONS AND SPECIAL RULES.—For purposes of this section—

"(1) FOREIGN-BASED DOCUMENTATION.—The term 'foreign-based documentation' means any documentation which is outside the United States and which may be relevent or material to the tax treatment of the examined item.

"(2) DOCUMENTATION.—The term 'documentation' includes books and records.

"(3) FOREIGN-CONNECTED.—An item shall be treated as foreign-connected if—

"(A) such item is directly or indirectly from a source outside the United States, or

"(B) such item (in whole or in part)—

"(i) purports to arise outside the United States, or

"(ii) is otherwise dependent on transactions occurring outside the United States.

"(4) AUTHORITY TO EXTEND 90-DAY PERIOD.—The Secretary, and any court having jurisdiction over a proceeding under subsection (c)(2), may extend the 90-day period referred to in subsection (a).

"(e) SUSPENSION OF STATUTE OF LIMITATIONS.—If any person takes any action as provided in subsection (c)(2), the running of any period of limitations under section 6501 (relating to the assessment and collection of tax) or under section 6531 (relating to criminal prosecutions) with respect to such person shall be suspended for the period during which the proceeding under such subsection, and appeals therein, are pending."

(b) CLERICAL AMENDMENT.—The table of subparts for part III of subchapter N of chapter 1 is amended by adding at the end thereof the following new item:

"Subpart I. Admissibility of documentation maintained in foreign countries."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply with respect to formal document requests (as defined in section 982(c)(1) of the Internal Revenue Code of 1954, as added by this section) mailed after the date of the enactment of this Act.

SEC. 338. PENALTY FOR FAILURE TO FURNISH INFORMATION WITH RESPECT TO CERTAIN FOREIGN CORPORATIONS.

(a) In General.—Section 6038 (relating to information with respect to certain foreign corporations) is amended by redesignating subsections (b), (c), and (d) as subsections (c), (d), and (e), respectively, and by inserting after subsection (a) the following new subsection:

"(b) Dollar Penalty for Failure To Furnish Information.—

"(1) In general.—If any person fails to furnish, within the time prescribed under paragraph (2) of subsection (a), any information with respect to any foreign corporation required under paragraph (1) of subsection (a), such person shall pay a penalty of $1,000 for each annual accounting period with respect to which such failure exists.

"(2) Increase in penalty where failure continues after notification.—If any failure described in paragraph (1) continues for more than 90 days after the day on which the Secretary mails notice of such failure to the United States person, such person shall pay a penalty (in addition to the amount required under paragraph (1)) of $1,000 for each 30-day period (or fraction thereof) during which such failure continues with respect to any annual accounting period after the expiration of such 90-day period. The increase in any penalty under this paragraph shall not exceed $24,000."

(b) Coordination With Existing Reduction in Foreign Tax Credit.—Subsection (c) of section 6038 (as redesignated by subsection (a)) is amended—

(1) by inserting "and subsection (b)" after "subsection" in paragraph (3)(B), and

(2) by redesignating paragraph (3) as paragraph (4) and by inserting after paragraph (2) the following new paragraph:

"(3) Coordination with subsection (b).—The amount of the reduction which (but for this paragraph) would be made under paragraph (1) with respect to any annual accounting period shall be reduced by the amount of the penalty imposed by subsection (b) with respect to such period."

(c) Technical Amendments.—

(1) The subsection heading of subsection (c) of section 6038 (as redesignated by subsection (a)) is amended to read as follows:

"(c) Penalty of Reducing Foreign Tax Credit.—".

(2) Paragraph (1) of section 6038(a) is amended by striking out "within the meaning of subsection (d)(1)" and inserting in lieu thereof "within the meaning of subsection (e)(1)".

(3) The last sentence of paragraph (1) of section 6038(c) (as redesignated by subsection (a)) is amended by inserting "of such failure" after "notice".

(d) Effective Date.—The amendments made by this section shall apply with respect to information for annual accounting periods ending after the date of the enactment of this Act.

SEC. 339. INFORMATION REQUIREMENTS WITH RESPECT TO CERTAIN FOREIGN-OWNED CORPORATIONS.

(a) General Rule.—Subpart A of part III of subchapter A of chapter 61 is amended by inserting after section 6038 the following new section:

"SEC. 6038A. INFORMATION WITH RESPECT TO CERTAIN FOREIGN-OWNED CORPORATIONS.

"(a) REQUIREMENT.—If, at any time during a taxable year, a corporation (hereinafter in this section referred to as the 'reporting corporation')—

"(1) is a domestic corporation or is a foreign corporation engaged in trade or business within the United States, and

"(2) is controlled by a foreign person,

such corporation shall furnish, at such time and in such manner as the Secretary shall by regulations prescribe, the information described in subsection (b).

"(b) REQUIRED INFORMATION.—For purposes of subsection (a), the information described in this subsection is such information as the Secretary may prescribe by regulations relating to—

"(1) the name, principal place of business, nature of business, and country or countries in which organized or resident, of each corporation which—

"(A) is a member of the same controlled group as the reporting corporation, and

"(B) had any transaction with the reporting corporation during its taxable year,

"(2) the manner in which the reporting corporation is related to each corporation referred to in paragraph (1), and

"(3) transactions between the reporting corporation and each foreign corporation which is a member of the same controlled group as the reporting corporation.

"(c) DEFINITIONS.—For purposes of this section—

"(1) CONTROL.—The term 'control' has the meaning given to such term by section 6038(d)(1); except that 'at least 50 percent' shall be substituted for 'more than 50 percent' each place it appears in such section.

"(2) CONTROLLED GROUP.—The term 'controlled group' means any controlled group of corporations within the meaning of section 1563(a); except that—

"(A) 'at least 50 percent' shall be substituted—

"(i) for 'at least 80 percent' each place it appears in section 1563(a)(1), and

"(ii) for 'more than 50 percent' each place it appears in section 1563(a)(2)(B), and

"(B) the determination shall be made without regard to subsections (a)(4) and (e)(3)(C) of section 1563.

"(3) FOREIGN PERSON.—The term 'foreign person' means any person who is not a United States person. For purposes of the preceding sentence, the term 'United States person' has the meaning given to such term by section 7701(a)(30); except that any individual who is a citizen of any possession of the United States (but not otherwise a citizen of the United States) and who is not a resident of the United States shall not be treated as a United States person.

"(d) PENALTY FOR FAILURE TO FURNISH INFORMATION.—

"(1) IN GENERAL.—If a reporting corporation fails to furnish (within the time prescribed by regulations) any information described in subsection (b), such corporation shall pay a penalty of

$1,000 for each taxable year with respect to which such failure occurs.

"(2) INCREASE IN PENALTY WHERE FAILURE CONTINUES AFTER NOTIFICATION.—If any failure described in paragraph (1) continues for more than 90 days after the day on which the Secretary mails notice of such failure to the reporting corporation, such corporation shall pay a penalty (in addition to the amount required under paragraph (1)) of $1,000 for each 30-day period (or fraction thereof) during which such failure continues after the expiration of such 90-day period. The increase in any penalty under this paragraph shall not exceed $24,000.

"(3) REASONABLE CAUSE.—For purposes of this subsection, the time prescribed by regulations to furnish information (and the beginning of the 90-day period after notice by the Secretary) shall be treated as not earlier than the last day on which (as shown to the satisfaction of the Secretary) reasonable cause existed for failure to furnish the information.

"(e) CROSS REFERENCE.—

> ***"For provisions relating to criminal penalties for violation of this section, see section 7203."***

(b) CLERICAL AMENDMENT.—The table of sections for subpart A of part III of subchapter A of chapter 61 is amended by inserting the following new item after the item relating to section 6038:

> *"Sec. 6038A. Information with respect to certain foreign-owned corporations."*

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to taxable years beginning after December 31, 1982.

SEC. 340. RETURNS WITH RESPECT TO FOREIGN PERSONAL HOLDING COMPANIES.

(a) GENERAL RULE.—Section 6035 (relating to returns of officers, directors, and shareholders of foreign personal holding companies) is amended to read as follows:

"SEC. 6035. RETURNS OF OFFICERS, DIRECTORS, AND SHAREHOLDERS OF FOREIGN PERSONAL HOLDING COMPANIES.

"(a) GENERAL RULE.—Each United States citizen or resident who is an officer, director, or 10-percent shareholder of a corporation which was a foreign personal holding company (as defined in section 552) for any taxable year shall file a return with respect to such taxable year setting forth—

"(1) the shareholder information required by subsection (b),

"(2) the income information required by subsection (c), and

"(3) such other information with respect to such corporation as the Secretary shall by forms or regulations prescribe as necessary for carrying out the purposes of this title.

"(b) SHAREHOLDER INFORMATION.—The shareholder information required by this subsection with respect to any taxable year shall be—

"(1) the name and address of each person who at any time during such taxable year held any share in the corporation,

"(2) a description of each class of shares and the total number of shares of such class outstanding at the close of the taxable year,

"(3) the number of shares of each class held by each person, and

"(4) any changes in the holdings of shares during the taxable year.

For purposes of paragraphs (1), (3), and (4), the term 'share' includes any security convertible into a share in the corporation and any option granted by the corporation with respect to any share in the corporation.

"(c) INCOME INFORMATION.—The income information required by this subsection for any taxable year shall be the gross income, deductions, credits, taxable income, and undistributed foreign personal holding company income of the corporation for the taxable year.

"(d) TIME AND MANNER FOR FURNISHING INFORMATION.—The information required under subsection (a) shall be furnished at such time and in such manner as the Secretary shall by forms and regulations prescribe.

"(e) DEFINITION AND SPECIAL RULES.—

"(1) 10-PERCENT SHAREHOLDER.—For purposes of this section, the term '10-percent shareholder' means any individual who owns directly or indirectly (within the meaning of section 554) 10 percent or more in value of the outstanding stock of a foreign corporation.

"(2) TIME FOR MAKING DETERMINATIONS.—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the determination of whether any person is an officer, director, or 10-percent shareholder with respect to any foreign corporation shall be made as of the date on which the return is required to be filed.

"(B) SPECIAL RULE.—If after the application of subparagraph (A) no person is required to file a return under subsection (a) with respect to any foreign corporation for any taxable year, the determination of whether any person is an officer, director, or 10-percent shareholder with respect to such foreign corporation shall be made on the last day of such taxable year on which there was such a person who was a United States citizen or resident.

"(3) 2 OR MORE PERSONS REQUIRED TO FURNISH INFORMATION WITH RESPECT TO SAME FOREIGN CORPORATION.—If, but for this paragraph, 2 or more persons would be required to furnish information under subsection (a) with respect to the same foreign corporation for the same taxable year, the Secretary may by regulations provide that such information shall be required only from 1 person."

(b) APPLICATION OF PENALTY.—

(1) Subsection (a) of section 6679 is amended by striking out "section 6046" and inserting in lieu thereof "section 6035 or 6046".

(2) The section heading for section 6679 is amended to read as follows:

"SEC. 6679. FAILURE TO FILE RETURNS OR SUPPLY INFORMATION UNDER SECTION 6035 OR 6046."

(3) The item relating to section 6679 in the table of sections for subchapter B of chapter 68 is amended to read as follows:

"Sec. 6679. Failure to file returns or supply information under section 6035 or 6046."

(c) Effective Date.—The amendment made by this section shall apply to taxable years of foreign corporations beginning after the date of the enactment of this Act.

SEC. 341. AUTHORITY TO DELAY DATE FOR FILING CERTAIN RETURNS RELATING TO FOREIGN CORPORATIONS AND FOREIGN TRUSTS.

(a) Foreign Corporations.—Subsection (d) of section 6046 (relating to time for filing returns as to organization or reorganization of foreign corporations and as to acquisitions of their stock) is amended by inserting before the period at the end thereof the following: "(or on or before such later day as the Secretary may by forms or regulations prescribe)".

(b) Foreign Trusts.—Subsection (a) of section 6048 (relating to returns as to certain foreign trusts) is amended by inserting "(or on or before such later day as the Secretary may by regulations prescribe)" after "the 90th day".

(c) Effective Date.—The amendments made by this section shall apply to returns filed after the date of the enactment of this Act.

SEC. 342. WITHHOLDING OF TAX ON NONRESIDENT ALIENS AND FOREIGN CORPORATIONS.

Not later than 2 years after the date of the enactment of this Act, the Secretary of the Treasury or his delegate shall prescribe regulations establishing certification procedures, refund procedures, or other procedures which ensure that any benefit of any treaty relating to withholding of tax under sections 1441 and 1442 of the Internal Revenue Code of 1954 is available only to persons entitled to such benefit.

SEC. 343. TECHNICAL AMENDMENT RELATING TO PENALTY UNDER SECTION 905(c).

(a) General Rule.—Subsection (c) of section 905 (relating to adjustments on payment of accrued taxes) is amended by striking out the last sentence.

(b) Effective Date.—The amendment made by subsection (a) shall have the same effect as if the last sentence of section 905(c) had never been enacted.

Subtitle G—Modification of Interest Provisions

SEC. 344. INTEREST COMPOUNDED DAILY.

(a) In General.—Subchapter C of chapter 67 (relating to determination of rate of interest) is amended by adding at the end thereof the following new section:

"SEC. 6622. INTEREST COMPOUNDED DAILY.

"(a) General Rule.—In computing the amount of any interest required to be paid under this title or sections 1961(c)(1) or 2411 of title 28, United States Code, by the Secretary or by the taxpayer, or any other amount determined by reference to such amount of interest, such interest and such amount shall be compounded daily.

"(b) Exception for Penalty for Failure To File Estimated Tax.—Subsection (a) shall not apply for purposes of computing the amount of any addition to tax under section 6654 or 6655."

(b) Conforming Amendments.—

(1) Section 6601(e) (relating to applicable rules) is amended by striking out paragraph (2) and redesignating paragraphs (3) and (4) as paragraphs (2) and (3), respectively.

(2) The table of sections for subchapter C of chapter 67 is amended by inserting after section 6621 the following new item:

"Sec. 6622. Interest compounded daily."

(3)(A) The heading for subchapter C of chapter 67 is amended by inserting "; Compounding of Interest" after "Rate".

(B) The item relating to subchapter C in the table of subchapters for chapter 67 is amended by inserting "; compounding of interest" after "rate".

(c) Effective Date.—The amendments made by this section shall apply to interest accruing after December 31, 1982.

SEC. 345. DETERMINATION OF RATE OF INTEREST TO BE MADE SEMIANNUALLY.

(a) In General.—Subsection (b) of section 6621 (relating to determination of rate of interest) is amended to read as follows:

"(b) Adjustment of Interest Rate.—

"(1) Establishment of adjusted rate.—If the adjusted prime rate charged by banks (rounded to the nearest full percent)—

"(A) during the 6-month period ending on September 30 of any calendar year, or

"(B) during the 6-month period ending on March 31 of any calendar year,

differs from the interest rate in effect under this section on either such date, respectively, then the Secretary shall establish, within 15 days after the close of the applicable 6-month period, an adjusted rate of interest equal to such adjusted prime rate.

"(2) Effective date of adjustment.—Any adjusted rate of interest established under paragraph (1) shall become effective—

"(A) on January 1 of the succeeding year in the case of an adjustment attributable to paragraph (1)(A), and

"(B) on July 1 of the same year in the case of an adjustment attributable to paragraph(1)(B)."

(b) Effective Date.—The amendment made by this section shall apply to adjustments taking effect on January 1, 1983.

SEC. 346. RESTRICTIONS ON PAYMENT OF INTEREST FOR CERTAIN PERIODS.

(a) Interest With Respect to Delinquent Returns.—Section 6611(b) (relating to period for which interest on refunds is paid) is amended by adding at the end thereof the following new paragraph:

"(3) Late returns.—Notwithstanding paragraph (1) or (2) in the case of a return of tax which is filed after the last date prescribed for filing such return (determined with regard to extensions), no interest shall be allowed or paid for any day before the date on which the return is filed."

(b) No Interest if Return Not in Processible Form.—Section 6611 (relating to interest on overpayments) is amended by redesignating subsection (i) as subsection (j) and by adding after subsection (h) the following new subsection:

“(i) No Interest Until Return in Processible Form.—

“(1) For purposes of subsections (b)(3), (e), and (h), a return shall not be treated as filed until it is filed in processible form.

“(2) For purposes of paragraph (1), a return is in a processible form if—

“(A) such return is filed on a permitted form, and

“(B) such return contains—

“(i) the taxpayer’s name, address, and identifying number and the required signature, and

“(ii) sufficient required information (whether on the return or on required attachments) to permit the mathematical verification of tax liability shown on the return.”

(c) Modification of Interest in the Case of Carrybacks.—

(1) Overpayments.—

(A) Paragraph (1) of section 6611(f) (relating to refund of income tax caused by carryback or adjustment for unused deductions) is amended by striking out “the close of the taxable year” and inserting in lieu thereof “the filing date for the taxable year”.

(B) Subparagraph (A) of section 6611(f)(2) is amended by striking out “the close of” each place it appears and inserting in lieu thereof “the filing date for”.

(C) Subsection (f) of section 6611 is amended by redesignating paragraph (3) as paragraph (4) and by inserting after paragraph (2) the following new paragraph:

“(3) Special rules for paragraphs (1) and (2).—

“(A) Filing date.—For purposes of this subsection, the term ‘filing date’ means the last date prescribed for filing the return of tax imposed by subtitle A for the taxable year (determined without regard to extensions).

“(B) Coordination with subsection (e).—

“(i) In general.—For purposes of subsection (e)—

“(I) any overpayment described in paragraph (1) or (2) shall be treated as an overpayment for the loss year, and

“(II) such subsection shall be applied with respect to such overpayment by treating the return for the loss year as not filed before claim for such overpayment is filed.

“(ii) Loss year.—For purposes of this subparagraph, the term ‘loss year’ means—

“(I) in the case of a carryback of a net operating loss or net capital loss, the taxable year in which such loss arises, and

“(II) in the case of a credit carryback, the taxable year in which such credit carryback arises (or, with respect to any portion of a credit carryback from a taxable year attributable to a net operating loss carryback, a capital loss carryback, or other credit carryback from a subsequent taxable year, such subsequent taxable year).”

(D) Subsection (g) of section 6611 is amended by striking out "the close of the taxable year" and inserting in lieu thereof "the filing date (as defined in subsection (f)(3)) for the taxable year".

(2) Underpayments.—

(A) Paragraph (1) of section 6601(d) (relating to income tax reduced by carryback for adjustment for certain unused deductions) is amended by striking out "the last day of the taxable year" and inserting in lieu thereof "the filing date for the taxable year".

(B) Subparagraph (A) of section 6601(d)(2) is amended by striking out "the last day of the" each place it appears and inserting in lieu thereof "the filing date for".

(C) Subsection (d) of section 6601 is amended by adding at the end thereof the following new paragraph:

"(4) Filing date.—For purposes of this subsection, the term 'filing date' has the meaning given to such term by section 6611(f)(3)(A)."

(d) Effective Dates.—

(1) In general.—The amendments made by subsections (a) and (b) shall apply to returns filed after the 30th day after the date of the enactment of this Act.

(2) Subsection (c).—The amendments made by subsection (c) shall apply to interest accruing after the 30th day after the date of the enactment of this Act.

Subtitle H—Taxpayer Safeguard Amendments

SEC. 347. INCREASE IN CERTAIN EXEMPTIONS FROM LEVY.

(a) General Rule.—

(1) Fuel, provisions, furniture, and personal effects.—Paragraph (2) of section 6334(a) (relating to property exempt from levy) is amended by striking out "$500" and inserting in lieu thereof "$1,500".

(2) Books and tools of a trade, business, or profession.—Paragraph (3) of section 6334(a) is amended by striking out "$250" and inserting in lieu thereof "$1,000".

(3) Wages, salary, or other income.—Paragraph (1) of section 6334(d) (relating to exempt amount of wages, salary, or other income) is amended—

(A) by striking out "$50" and inserting in lieu thereof "$75", and

(B) by striking out "$15" and inserting in lieu thereof "$25".

(b) Effective Date.—The amendments made by subsection (a) shall apply to levies made after December 31, 1982.

SEC. 348. REQUIRED RELEASE OF LIEN.

(a) General Rule.—So much of subsection (a) of section 6325 (relating to release of lien) as precedes paragraph (1) thereof is amended to read as follows:

"(a) Release of Lien.—Subject to such regulations as the Secretary may prescribe, the Secretary shall issue a certificate of release

of any lien imposed with respect to any internal revenue tax not later than 30 days after the day on which—".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to liens—

(1) which are filed after December 31, 1982,

(2) which are satisfied after December 31, 1982, or

(3) with respect to which the taxpayer after December 31, 1982, requests the Secretary of the Treasury or his delegate to issue a certificate of release on the grounds that the liability was satisfied or legally unenforceable.

SEC. 349. REQUIREMENT OF TIMELY NOTICE OF LEVY.

(a) GENERAL RULE.—Section 6331 (relating to levy and distraint) is amended by redesignating subsection (e) as subsection (f) and by striking out subsection (d) and inserting in lieu thereof the following new subsections:

"(d) REQUIREMENT OF NOTICE BEFORE LEVY.—

"(1) IN GENERAL.—Levy may be made under subsection (a) upon the salary or wages or other property of any person with respect to any unpaid tax only after the Secretary has notified such person in writing of his intention to make such levy.

"(2) 10-DAY REQUIREMENT.—The notice required under paragraph (1) shall be—

"(A) given in person,

"(B) left at the dwelling or usual place of business of such person, or

"(C) sent by certified or registered mail to such person's last known address,

no less than 10 days before the day of the levy.

"(3) JEOPARDY.—Paragraph (1) shall not apply to a levy if the Secretary has made a finding under the last sentence of subsection (a) that the collection of tax is in jeopardy.

"(e) CONTINUING LEVY ON SALARY AND WAGES.—

"(1) EFFECT OF LEVY.—The effect of a levy on salary or wages payable to or received by a taxpayer shall be continuous from the date such levy is first made until the liability out of which such levy arose is satisfied or becomes unenforceable by reason of lapse of time.

"(2) RELEASE AND NOTICE OF RELEASE.—With respect to a levy described in paragraph (1), the Secretary shall promptly release the levy when the liability out of which such levy arose is satisfied or becomes unenforceable by reason of lapse of time, and shall promptly notify the person upon whom such levy was made that such levy has been released."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply to levies made after December 31, 1982.

SEC. 349A. EXTENSION OF PERIOD FOR REDEMPTION OF REAL PROPERTY.

(a) GENERAL RULE.—Paragraph (1) of section 6337(b) (relating to period for redemption of real estate after sale) is amended by striking out "120 days" and inserting in lieu thereof "180 days".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to property sold after the date of the enactment of this Act.

SEC. 350. AMOUNT OF DAMAGES IN CASE OF WRONGFUL LEVY.

(a) GENERAL RULE.—Subparagraph (C) of section 7426(b)(2) (relating to amount of damages) is amended to read as follows:

"(C) if such property was sold, grant a judgment for an amount not exceeding the greater of—

"(i) the amount received by the United States from the sale of such property, or

"(ii) the fair market value of such property immediately before the levy."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to levies made after December 31, 1982.

Subtitle I—Other Provisions

SEC. 351. DISALLOWANCE OF DEDUCTIONS RELATING TO NARCOTICS TRAFFICKING.

(a) IN GENERAL.—Part IX of subchapter B of chapter 1 (relating to items not deductible) is amended by adding at the end thereof the following new section:

"SEC. 280E. EXPENDITURES IN CONNECTION WITH THE ILLEGAL SALE OF DRUGS.

"No deduction or credit shall be allowed for any amount paid or incurred during the taxable year in carrying on any trade or business if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances (within the meaning of schedule I and II of the Controlled Substances Act) which is prohibited by Federal law or the law of any State in which such trade or business is conducted."

(b) CONFORMING AMENDMENT.—The table of sections for part IX of subchapter B of chapter 1 of such Code is amended by adding at the end thereof the following new item:

"Sec. 280E. Expenditures in connection with the illegal sale of drugs."

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to amounts paid or incurred after the date of the enactment of this Act in taxable years ending after such date.

SEC. 352. SENSE OF CONGRESS WITH RESPECT TO PROVIDING OF ADDITIONAL FUNDS TO INTERNAL REVENUE SERVICE.

It is the sense of the Congress that there be appropriated for the use of the Internal Revenue Service to provide additional staff—

(1) for fiscal year 1983, the amounts proposed in the President's budget for fiscal year 1983, and

(2) such amounts in excess of the amount requested for such purpose in the President's proposed budgets as may be necessary to provide sufficient improved enforcement to increase revenues by $1 billion in fiscal year 1984 and $2 billion in fiscal year 1985.

SEC. 353. REPORT ON FORMS.

Not later than June 30, 1983, the Secretary of the Treasury or his delegate shall study and report to the Congress methods of modifying the design of the forms used by the Internal Revenue Service to achieve greater accuracy in the reporting of income and the match-

ing of information reports and returns with the returns of tax imposed by chapter 1 of the Internal Revenue Code of 1954.

SEC. 354. EXEMPTION OF VETERANS' ORGANIZATIONS.

(a) IN GENERAL.—Paragraph (19) of section 501(c) (relating to exemption of veterans' organizations) is amended—

(1) by striking out "war veterans" the first place it appears and inserting in lieu thereof "past or present members of the Armed Forces of the United States", and

(2) by amending subparagraph (B) to read as follows:

"(B) at least 75 percent of the members of which are past or present members of the Armed Forces of the United States and substantially all of the other members of which are individuals who are cadets or are spouses, widows, or widowers of past or present members of the Armed Forces of the United States or of cadets, and".

(b) ASSOCIATION ORGANIZED BEFORE 1880.—Subsection (c) of section 501 (relating to exempt organizations) is amended by adding at the end thereof the following new paragraph:

"(23) any association organized before 1880 more than 25 percent of the members of which are present or past members of the Armed Forces and a principal purpose of which is to provide insurance and other benefits to veterans or their dependents."

(c) EFFECTIVE DATE.—The amendments made by subsections (a) and (b) shall apply to taxable years beginning after the date of the enactment of this Act.

SEC. 355. AMENDMENT TO COMMUNICATIONS ACT OF 1934.

Title III of the Communications Act of 1934 is amended by inserting immediately after section 330 therein the following new section:

"VERY HIGH FREQUENCY STATIONS

"SEC. 331. It shall be the policy of the Federal Communications Commission to allocate channels for very high frequency commercial television broadcasting in a manner which ensures that not less than one such channel shall be allocated to each State, if technically feasible. In any case in which licensee of a very high frequency commercial television broadcast station notifies the Commission to the effect that such licensee will agree to the reallocation of its channel to a community within a State in which there is allocated no very high frequency commercial television broadcast channel at the time such notification, the Commission shall, notwithstanding any other provision of law, order such reallocation and issue a license to such licensee for that purpose pursuant to such notification for a term of not to exceed 5 years as provided in section 307(d) of the Communications Act of 1934."

SEC. 356. CONFIDENTIALITY AND DISCLOSURE OF RETURNS AND RETURN INFORMATION.

(a) IN GENERAL.— Subsection (i) of section 6103 (relating to disclosure to Federal officers or employees for administration of Federal laws not relating to tax administration) is amended by redesignating paragraph (6) as paragraph (7) and by striking out paragraphs (1), (2), (3), (4), and (5) and inserting in lieu thereof the following:

"(1) Disclosure of returns and return information for use in criminal investigations.—

"(A) In general.—Except as provided in paragraph (6), any return or return information with respect to any specified taxable period or periods shall, pursuant to and upon the grant of an ex parte order by a Federal district court judge or magistrate under subparagraph (B), be open (but only to the extent necessary as provided in such order) to inspection by, or disclosure to, officers and employees of any Federal agency who are personally and directly engaged in—

"(i) preparation for any judicial or administrative proceeding pertaining to the enforcement of a specifically designated Federal criminal statute (not involving tax administration) to which the United States or such agency is or may be a party,

"(ii) any investigation which may result in such a proceeding, or

"(iii) any Federal grand jury proceeding pertaining to enforcement of such a criminal statute to which the United States or such agency is or may be a party,

solely for the use of such officers and employees in such preparation, investigation, or grand jury proceeding.

"(B) Application for order.—The Attorney General, the Deputy Attorney General, the Associate Attorney General, any Assistant Attorney General, any United States attorney, any special prosecutor appointed under section 593 of title 28, United States Code, or any attorney in charge of a criminal division organized crime strike force established pursuant to section 510 of title 28, United States Code, may authorize an application to a Federal district court judge or magistrate for the order referred to in subparagraph (A). Upon such application, such judge or magistrate may grant such order if he determines on the basis of the facts submitted by the applicant that—

"(i) there is reasonable cause to believe, based upon information believed to be reliable, that a specific criminal act has been committed,

"(ii) there is reasonable cause to believe that the return or return information is or may be relevant to a matter relating to the commission of such act, and

"(iii) the return or return information is sought exclusively for use in a Federal criminal investigation or proceeding concerning such act, and the information sought to be disclosed cannot reasonably be obtained, under the circumstances, from another source.

"(2) Disclosure of return information other than taxpayer return information for use in criminal investigations.—

"(A) In general.—Except as provided in paragraph (6), upon receipt by the Secretary of a request which meets the requirements of subparagraph (B) from the head of any Federal agency or the Inspector General thereof, or, in the

case of the Department of Justice, the Attorney General, the Deputy Attorney General, the Associate Attorney General, any Assistant Attorney General, the Director of the Federal Bureau of Investigation, the Administrator of the Drug Enforcement Administration, any United States attorney, any special prosecutor appointed under section 593 of title 28, United States Code, or any attorney in charge of a criminal division organized crime strike force established pursuant to section 510 of title 28, United States Code, the Secretary shall disclose return information (other than taxpayer return information) to officers and employees of such agency who are personally and directly engaged in—

"(i) preparation for any judicial or administrative proceeding described in paragraph (1)(A)(i),

"(ii) any investigation which may result in such a proceeding, or

"(iii) any grand jury proceeding described in paragraph (1)(A)(iii),

solely for the use of such officers and employees in such preparation, investigation, or grand jury proceeding.

"(B) Requirements.—A request meets the requirements of this subparagraph if the request is in writing and sets forth—

"(i) the name and address of the taxpayer with respect to whom the requested return information relates;

"(ii) the taxable period or periods to which such return information relates;

"(iii) the statutory authority under which the proceeding or investigation described in subparagraph (A) is being conducted; and

"(iv) the specific reason or reasons why such disclosure is, or may be, relevant to such proceeding or investigation.

"(C) Taxpayer identity.—For purposes of this paragraph, a taxpayer's identity shall not be treated as taxpayer return information.

"(3) Disclosure of return information to apprise appropriate officials of criminal activities or emergency circumstances.—

"(A) Possible violations of federal criminal law.—

"(i) In general.—Except as provided in paragraph (6), the Secretary may disclose in writing return information (other than taxpayer return information) which may constitute evidence of a violation of any Federal criminal law (not involving tax administration) to the extent necessary to apprise the head of the appropriate Federal agency charged with the responsibility of enforcing such law. The head of such agency may disclose such return information to officers and employees of such agency to the extent necessary to enforce such law.

"(ii) Taxpayer identity.—If there is return information (other than taxpayer return information) which may constitute evidence of a violation by any taxpayer of any Federal criminal law (not involving tax admin-

istration), such taxpayer's identity may also be disclosed under clause (i).

"(B) Emergency circumstances.—

"(i) Danger of death or physical injury.—Under circumstances involving an imminent danger of death or physical injury to any individual, the Secretary may disclose return information to the extent necessary to apprise appropriate officers or employees of any Federal or State law enforcement agency of such circumstances.

"(ii) Flight from federal prosecution.—Under circumstances involving the imminent flight of any individual from Federal prosecution, the Secretary may disclose return information to the extent necessary to apprise appropriate officers or employees of any Federal law enforcement agency of such circumstances.

"(4) Use of certain disclosed returns and return information in judicial or administrative proceedings.—

"(A) Returns and taxpayer return information.—Except as provided in subparagraph (c), any return or taxpayer return information obtained under paragraph (1) may be disclosed in any judicial or administrative proceeding pertaining to enforcement of a specifically designated Federal criminal statute or related civil forfeiture (not involving tax administration) to which the United States or a Federal agency is a party—

"(i) if the court finds that such return or taxpayer return information is probative of a matter in issue relevant in establishing the commissison of a crime or the guilt or liability of a party, or

"(ii) to the extent required by order of the court pursuant to section 3500 of title 18, United States Code, or rule 16 the Federal Rules of Criminal Procedure.

"(B) Return information (other than taxpayer return information).—Except as provided in subparagraph (C), any return information (other than taxpayer return information) obtained under paragraph (1), (2), or (3)(A) may be disclosed in any judicial or administrative proceeding pertaining to enforcement of a specifically designated Federal criminal statute or related civil forfeiture (not involving tax administration) to which the United States or a Federal agency is a party.

"(C) Confidential informant; impairment of investigations.—No return or return information shall be admitted into evidence under subparagraph (A)(i) or (B) if the Secretary determines and notifies the Attorney General or his delegate or the head of the Federal agency that such admission would identify a confidential informant or seriously impair a civil or criminal tax investigation.

"(D) Consideration of confidentiality policy.—In ruling upon the admissibility of returns or return information, and in the issuance of an order under subparagraph (A)(ii), the court shall give due consideration to congressional policy favoring the confidentiality of returns and return information as set forth in this title.

"(E) REVERSIBLE ERROR.—The admission into evidence of any return or return information contrary to the provisions of this paragraph shall not, as such, constitute reversible error upon appeal of a judgment in the proceeding.

"(5) DISCLOSURE TO LOCATE FUGITIVES FROM JUSTICE.—

"(A) IN GENERAL.—Except as provided in paragraph (6), the return of an individual or return information with respect to such individual shall, pursuant to and upon the grant of an ex parte order by a Federal district court judge or magistrate under subparagraph (B), be open (but only to the extent necessary as provided in such order) to inspection by, or disclosure to, officers and employees of any Federal agency exclusively for use in locating such individual.

"(B) APPLICATION FOR ORDER.—Any person described in paragraph (1)(B) may authorize an application to a Federal district court judge or magistrate for an order referred to in subparagraph (A). Upon such application, such judge or magistrate may grant such order if he determines on the basis of the facts submitted by the applicant that—

"(i) a Federal arrest warrant relating to the commission of a Federal felony offense has been issued for an individual who is a fugitive from justice,

"(ii) the return of such individual or return information with respect to such individual is sought exclusively for use in locating such individual, and

"(iii) there is reasonable cause to believe that such return or return information may be relevant in determining the location of such individual.

"(6) CONFIDENTIAL INFORMANTS; IMPAIRMENT OF INVESTIGATIONS.—The Secretary shall not disclose any return or return information under paragraph (1), (2), (3)(A), (5), or (7) if the Secretary determines (and, in the case of a request for disclosure pursuant to a court order described in paragraph (1)(B) or (5)(B), certifies to the court) that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.".

(b) CONFORMING AMENDMENTS.—

(1) Subsection (p) of section 6103 (relating to procedure and recordkeeping) is amended—

(A) by striking out "(6)(A)(ii)" in paragraph (3)(A) and inserting in lieu thereof "(7)(A)(ii)",

(B) by striking out "(d)" in paragraph (3)(C)(i) and inserting in lieu thereof "(d), (i)(3)(B)(i),",

(C) by striking out "such requests" in paragraph (3)(C)(i)(II) and inserting in lieu thereof "such requests or otherwise",

(D) by striking out "(i)(1), (2), or (5)" each place it appears in paragraph (4) and inserting in lieu thereof "(i)(1), (2), (3), or (5)",

(E) by striking out "(d)" each place it appears in paragraph (4) and inserting in lieu thereof "(d), (i)(3)(B)(i),", and

(F) by striking out "subsection (i)(6)(A)(ii)" in paragraph (6)(B)(i) and inserting in lieu thereof "subsection (i)(7)(A)(ii)".

(2) Paragraph (2) of section 7213(a) (relating to unauthorized disclosure of information) is amended by striking out "(d)" and inserting in lieu thereof "(d), (i)(3)(B)(i),".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the day after the date of the enactment of this Act.

SEC. 357. CIVIL DAMAGES AGAINST UNITED STATES FOR UNAUTHORIZED DISCLOSURES BY AN EMPLOYEE.

(a) IN GENERAL.—Subchapter B of chapter 76 (relating to proceedings by taxpayers and third parties) is amended by redesignating section 7431 as section 7432 and inserting after section 7430 the following new section:

"SEC. 7430. CIVIL DAMAGES FOR UNAUTHORIZED DISCLOSURE OF RETURNS AND RETURN INFORMATION.

"(a) IN GENERAL.—

"(1) DISCLOSURE BY EMPLOYEE OF UNITED STATES.—If any officer or employee of the United States knowingly, or by reason of negligence, discloses any return or return information with respect to a taxpayer in violation of any provision of section 6103, such taxpayer may bring a civil action for damages against the United States in a district court of the United States.

"(2) DISCLOSURE BY A PERSON WHO IS NOT AN EMPLOYEE OF UNITED STATES.—If any person who is not an officer or employee of the United States knowingly, or by reason of negligence, discloses any return or return information with respect to a taxpayer in violation of any provision of section 6103, such taxpayer may bring a civil action for damages against such person in a district court of the United States.

"(b) NO LIABILITY FOR GOOD FAITH BUT ERRONEOUS INTERPRETATION.—No liability shall arise under this section with respect to any disclosure which results from a good faith, but erroneous, interpretation of section 6103.

"(c) DAMAGES.—In any action brought under subsection (a), upon a finding of liability on the part of the defendant, the defendant shall be liable to the plaintiff in an amount equal to the sum of—

"(1) the greater of—

"(A) $1,000 for each act of unauthorized disclosure of a return or return information with respect to which such defendant is found liable, or

"(B) the sum of—

"(i) the actual damages sustained by the plaintiff as a result of such unauthorized disclosure, plus

"(ii) in the case of a willful disclosure or a disclosure which is the result of gross negligence, punitive damages, plus

"(2) the costs of the action.

"(d) PERIOD FOR BRINGING ACTION.—Notwithstanding any other provision of law, an action to enforce any liability created under this section may be brought, without regard to the amount in controversy, at any time within 2 years after the date of discovery by the plaintiff of the unauthorized disclosure.

"(e) Return; Return Information.—For purposes of this section, the terms 'return' and 'return information' have the respective meanings given such terms in section 6103(b)."

(b) Conforming Amendments.—

(1) Section 7217 (relating to civil damages for unauthorized disclosure of returns and return information) is hereby repealed.

(2) The table of sections for part I of subchapter A of chapter 75 is amended by striking out the item relating to section 7217.

(3) The table of sections for subchapter B of chapter 76 is amended by striking out the item relating to section 7431 and inserting in lieu thereof the following:

"Sec. 7431. Civil damages for unauthorized disclosure of returns and return information.
"Sec. 7432. Cross references."

(c) Effective Date.—The amendments made by this section shall apply with respect to disclosures made after the date of enactment of this Act.

SEC. 358. DISCLOSURE FOR USE IN CERTAIN AUDITS BY GENERAL ACCOUNTING OFFICE.

(a) In General.—Paragraph (7) of section 6103(i) (relating to disclosure to Comptroller General), as redesignated by section 396(a), is amended by redesignating subparagraph (B) as subparagraph (C) and by inserting after subparagraph (A) the following new subparagraph:

"(B) Audits of other agencies.—

"(i) In general.—Nothing in this section shall prohibit any return or return information obtained under this title by any Federal agency (other than an agency referred to in subparagraph (A)) for use in any program or activity from being open to inspection by, or disclosure to, officers and employees of the General Accounting Office if such inspection or disclosure is—

"(I) for purposes of, and to the extent necessary in, making an audit authorized by law of such program or activity, and

"(II) pursuant to a written request by the Comptroller General of the United States to the head of such Federal agency.

"(ii) Information from secretary.—If the Comptroller General of the United States determines that the returns or return information available under clause (i) are not sufficient for purposes of making an audit of any program or activity of a Federal agency (other than an agency referred to in subparagraph (A)), upon written request by the Comptroller General to the Secretary, returns and return information (of the type authorized by subsection (l) or (m) to be made available to the Federal agency for use in such program or activity) shall be open to inspection by, or disclosure to, officers and employees of the General Accounting Office for the purpose of, and to the extent necessary in, making such audit.

"(iii) REQUIREMENT OF NOTIFICATION UPON COMPLETION OF AUDIT.—Within 90 days after the completion of an audit with respect to which returns or return information were opened to inspection or disclosed under clause (i) or (ii), the Comptroller General of the United States shall notify in writing the Joint Committee on Taxation of such completion. Such notice shall include—

"(I) a description of the use of the returns and return information by the Federal agency involved,

"(II) such recommendations with respect to the use of returns and return information by such Federal agency as the Comptroller General deems appropriate, and

"(III) a statement on the impact of any such recommendations on confidentiality of returns and return information and the administration of this title.

"(iv) CERTAIN RESTRICTIONS MADE APPLICABLE.—The restrictions contained in subparagraph (A) on the disclosure of any returns or return information open to inspection or disclosed under such subparagraph shall also apply to returns and return information open to inspection or disclosed under this subparagraph."

(b) CONFORMING AMENDMENTS.—

(1) Subparagraph (A) of section 6103(i)(7) of such Code (as redesignated by this Act) is amended by striking out "subparagraph (B)" and inserting in lieu thereof "subparagraph (C)".

(2) Subparagraph (C) of section 6103(i)(7) of such Code (as redesignated by this Act) is amended by striking out "subparagraph (A)" and inserting in lieu thereof "subparagraph (A) or (B)".

(c) EFFECTIVE DATE.—The amendments made by this section shall take effect on the day after the date of the enactment of this Act.

TITLE IV—TAX TREATMENT OF PARTNERSHIP ITEMS

SEC. 401. SHORT TITLE.

This title may be cited as the "Tax Treatment of Partnership Items Act of 1982".

SEC. 402. TAX TREATMENT OF PARTNERSHIP ITEMS.

(a) GENERAL RULE.—Chapter 63 (relating to assessment) is amended by adding at the end thereof the following new subchapter:

"Subchapter C—Tax Treatment of Partnership Items

"Sec. 6221. Tax treatment determined at partnership level.
"Sec. 6222. Partner's return must be consistent with partnership return or Secretary notified of inconsistency.
"Sec. 6223. Notice to partners of proceedings.
"Sec. 6224. Participation in administrative proceedings; waivers; agreements.

"Sec. 6225. Assessments made only after partnership level proceedings are completed.
"Sec. 6226. Judicial review of final partnership administrative adjustments.
"Sec. 6227. Administrative adjustment requests.
"Sec. 6228. Judicial review where administrative adjustment request is not allowed in full.
"Sec. 6229. Period of limitations for making assessments.
"Sec. 6230. Additional administrative provisions.
"Sec. 6231. Definitions and special rules.
"Sec. 6232. Extension of subchapter to windfall profit tax.

"SEC. 6221. TAX TREATMENT DETERMINED AT PARTNERSHIP LEVEL.

"Except as otherwise provided in this subchapter, the tax treatment of any partnership item shall be determined at the partnership level.

"SEC. 6222. PARTNER'S RETURN MUST BE CONSISTENT WITH PARTNERSHIP RETURN OR SECRETARY NOTIFIED OF INCONSISTENCY.

"(a) In General.—A partner shall, on the partner's return, treat a partnership item in a manner which is consistent with the treatment of such partnership item on the partnership return.

"(b) Notification of Inconsistent Treatment.—

"(1) In general.—In the case of any partnership item, if—

"(A)(i) the partnership has filed a return but the partner's treatment on his return is (or may be) inconsistent with the treatment of the item on the partnership return, or

"(ii) the partnership has not filed a return, and

"(B) the partner files with the Secretary a statement identifying the inconsistency,

subsection (a) shall not apply to such item.

"(2) Partner receiving incorrect information.—A partner shall be treated as having complied with subparagraph (B) of paragraph (1) with respect to a partnership item if the partner—

"(A) demonstrates to the satisfaction of the Secretary that the treatment of the partnership item on the partner's return is consistent with the treatment of the item on the schedule furnished to the partner by the partnership, and

"(B) elects to have this paragraph apply with respect to that item.

"(c) Effect of Failure To Notify.—In any case—

"(1) described in paragraph (1)(A)(i) of subsection (b), and

"(2) in which the partner does not comply with paragraph (1)(B) of subsection (b),

section 6225 shall not apply to any part of a deficiency attributable to any computational adjustment required to make the treatment of the items by such partner consistent with the treatment of the items on the partnership return.

"(d) Addition to Tax for Failure To Comply With Section.—

"For addition to tax in the case of a partner's intentional or negligent disregard of requirements of this section, see section 6653(a).

"SEC. 6223. NOTICE TO PARTNERS OF PROCEEDINGS.

"(a) Secretary Must Give Partners Notice of Beginning and Completion of Administrative Proceedings.—The Secretary shall mail to each partner whose name and address is furnished to the Secretary notice of—

"(1) the beginning of an administrative proceeding at the partnership level with respect to a partnership item, and

"(2) the final partnership administrative adjustment resulting from any such proceeding.

A partner shall not be entitled to any notice under this subsection unless the Secretary has received (at least 30 days before it is mailed to the tax matters partner) sufficient information to enable the Secretary to determine that such partner is entitled to such notice and to provide such notice to such partner.

"(b) SPECIAL RULES FOR PARTNERSHIP WITH MORE THAN 100 PARTNERS.—

"(1) PARTNER WITH LESS THAN 1 PERCENT INTEREST.—Except as provided in paragraph (2), subsection (a) shall not apply to a partner if—

"(A) the partnership has more than 100 partners, and

"(B) the partner has a less than 1 percent interest in the profits of the partnership.

"(2) SECRETARY MUST GIVE NOTICE TO NOTICE GROUP.—If a group of partners in the aggregate having a 5 percent or more interest in the profits of a partnership so request and designate one of their members to receive the notice, the member so designated shall be treated as a partner to whom subsection (a) applies.

"(c) INFORMATION BASE FOR SECRETARY'S NOTICES, ETC.—For purposes of this subchapter—

"(1) INFORMATION ON PARTNERSHIP RETURN.—Except as provided in paragraphs (2) and (3), the Secretary shall use the names, addresses, and profits interests shown on the partnership return.

"(2) USE OF ADDITIONAL INFORMATION.—The Secretary shall use additional information furnished to him by the tax matters partner or any other person in accordance with regulations prescribed by the Secretary.

"(3) SPECIAL RULE WITH RESPECT TO INDIRECT PARTNERS.—If any information furnished to the Secretary under paragraph (1) or (2)—

"(A) shows that a person has a profits interest in the partnership by reason of ownership of an interest through 1 or more pass-thru partners, and

"(B) contains the name, address, and profits interest of such person,

then the Secretary shall use the name, address, and profits interest of such person with respect to such partnership interest (in lieu of the names, addresses, and profits interests of the pass-thru partners).

"(d) PERIOD FOR MAILING NOTICE.—

"(1) NOTICE OF BEGINNING OF PROCEEDINGS.—The Secretary shall mail the notice specified in paragraph (1) of subsection (a) to each partner entitled to such notice not later than the 120th day before the day on which the notice specified in paragraph (2) of subsection (a) is mailed to the tax matters partner.

"(2) NOTICE OF FINAL PARTNERSHIP ADMINISTRATIVE ADJUSTMENT.—The Secretary shall mail the notice specified in paragraph (2) of subsection (a) to each partner entitled to such notice

not later than the 60th day after the day on which the notice specified in such paragraph (2) was mailed to the tax matters partner.

"(e) EFFECT OF SECRETARY'S FAILURE TO PROVIDE NOTICE.—

"(1) APPLICATION OF SUBSECTION.—

"(A) IN GENERAL.—This subsection applies where the Secretary has failed to mail any notice specified in subsection (a) to a partner entitled to such notice within the period specified in subsection (d).

"(B) SPECIAL RULES FOR PARTNERSHIPS WITH MORE THAN 100 PARTNERS.—For purposes of subparagraph (A), any partner described in paragraph (1) of subsection (b) shall be treated as entitled to notice specified in subsection (a). The Secretary may provide such notice—

"(i) except as provided in clause (ii), by mailing notice to the tax matters partner, or

"(ii) in the case of a member of a notice group which qualifies under paragraph (2) of subsection (b), by mailing notice to the partner designated for such purpose by the group.

"(2) PROCEEDINGS FINISHED.—In any case to which this subsection applies, if at the time the Secretary mails the partner notice of the proceeding—

"(A) the period within which a petition for review of a final partnership administrative adjustment under section 6226 may be filed has expired and no such petition has been filed, or

"(B) the decision of a court in an action begun by such a petition has become final,

the partner may elect to have such adjustment, such decision, or a settlement agreement described in paragraph (2) of section 6224(c) with respect to the partnership taxable year to which the adjustment relates apply to such partner. If the partner does not make an election under the preceding sentence, the partnership items of the partner for the partnership taxable year to which the proceeding relates shall be treated as nonpartnership items.

"(3) PROCEEDINGS STILL GOING ON.—In any case to which this subsection applies, if paragraph (2) does not apply, the partner shall be a party to the proceeding unless such partner elects—

"(A) to have a settlement agreement described in paragraph (2) of section 6224(c) with respect to the partnership taxable year to which the proceeding relates apply to the partner, or

"(B) to have the partnership items of the partner for the partnership taxable year to which the proceeding relates treated as nonpartnership items.

"(f) ONLY ONE NOTICE OF FINAL PARTNERSHIP ADMINISTRATIVE ADJUSTMENT.—If the Secretary mails a notice of final partnership administrative adjustment for a partnership taxable year with respect to a partner, the Secretary may not mail another such notice to such partner with respect to the same taxable year of the same partnership in the absence of a showing of fraud, malfeasance, or misrepresentation of a material fact.

"(g) TAX MATTERS PARTNER MUST KEEP PARTNERS INFORMED OF PROCEEDINGS.—To the extent and in the manner provided by regulations, the tax matters partner of a partnership shall keep each partner informed of all administrative and judicial proceedings for the adjustment at the partnership level of partnership items.

"(h) PASS-THRU PARTNER REQUIRED TO FORWARD NOTICE.—

"(1) IN GENERAL.—If a pass-thru partner receives a notice with respect to a partnership proceeding from the Secretary, the tax matters partner, or another pass-thru partner, the pass-thru partner shall, within 30 days of receiving that notice, forward a copy of that notice to the person or persons holding an interest (through the pass-thru partner) in the profits or losses of the partnership for the partnership taxable year to which the notice relates.

"(2) PARTNERSHIP AS PASS-THRU PARTNER.—In the case of a pass-thru partner which is a partnership, the tax matters partner of such partnership shall be responsible for forwarding copies of the notice to the partners of such partnership.

"SEC. 6224. PARTICIPATION IN ADMINISTRATIVE PROCEEDINGS; WAIVERS; AGREEMENTS.

"(a) PARTICIPATION IN ADMINISTRATIVE PROCEEDINGS.—Any partner has the right to participate in any administrative proceeding relating to the determination of partnership items at the partnership level.

"(b) PARTNER MAY WAIVE RIGHTS.—

"(1) IN GENERAL.—A partner may at any time waive—

"(A) any right such partner has under this subchapter, and

"(B) any restriction under this subchapter on action by the Secretary.

"(2) FORM.—Any waiver under paragraph (1) shall be made by a signed notice in writing filed with the Secretary.

"(c) SETTLEMENT AGREEMENT.—In the absence of a showing of fraud, malfeasance, or misrepresentation of fact—

"(1) BINDS ALL PARTIES.—A settlement agreement between the Secretary and 1 or more partners in a partnership with respect to the determination of partnership items for any partnership taxable year shall (except as otherwise provided in such agreement) be binding on all parties to such agreement with respect to the determination of partnership items for such partnership taxable year. An indirect partner is bound by any such agreement entered into by the pass-thru partner unless the indirect partner has been identified as provided in section 6223(c)(3).

"(2) OTHER PARTNERS HAVE RIGHT TO ENTER INTO CONSISTENT AGREEMENTS.—If the Secretary enters into a settlement agreement with any partner with respect to partnership items for any partnership taxable year, the Secretary shall offer to any other partner who so requests settlement terms for the partnership taxable year which are consistent with those contained in such settlement agreement. Except in the case of an election under paragraph (2) or (3) of section 6223(e) to have a settlement agreement described in this paragraph apply, this paragraph shall apply with respect to a settlement agreement entered into with a

partner before notice of a final partnership administrative adjustment is mailed to the tax matters partner only if such other partner makes the request before the expiration of 150 days after the day on which such notice is mailed to the tax matters partner.

"(3) Tax matters partner may bind certain other partners.—

"(A) In general.—A partner who is not a notice partner (and not a member of a notice group described in subsection (b)(2) of section 6223) shall be bound by any settlement agreement—

"(i) which is entered into by the tax matters partner, and

"(ii) in which the tax matters partner expressly states that such agreement shall bind the other partners.

"(B) Exception.—Subparagraph (A) shall not apply to any partner who (within the time prescribed by the Secretary) files a statement with the Secretary providing that the tax matters partner shall not have the authority to enter into a settlement agreement on behalf of such partner.

"SEC. 6225. ASSESSMENTS MADE ONLY AFTER PARTNERSHIP LEVEL PROCEEDINGS ARE COMPLETED.

"(a) Restriction on Assessment and Collection.—Except as otherwise provided in this subchapter, no assessment of a deficiency attributable to any partnership item may be made (and no levy or proceeding in any court for the collection of any such deficiency may be made, begun, or prosecuted) before—

"(1) the close of the 150th day after the day on which a notice of a final partnership administrative adjustment was mailed to the tax matters partner, and

"(2) if a proceeding is begun in the Tax Court under section 6226 during such 150-day period, the decision of the court in such proceeding has become final.

"(b) Premature Action May Be Enjoined.—Notwithstanding section 7421(a), any action which violates subsection (a) may be enjoined in the proper court.

"(c) Limit Where No Proceeding Begun.—If no proceeding under section 6226 is begun with respect to any final partnership administrative adjustment during the 150-day period described in subsection (a), the deficiency assessed against any partner with respect to the partnership items to which such adjustment relates shall not exceed the amount determined in accordance with such adjustment.

"SEC. 6226. JUDICIAL REVIEW OF FINAL PARTNERSHIP ADMINISTRATIVE ADJUSTMENTS.

"(a) Petition by Tax Matters Partner.—Within 90 days after the day on which a notice of a final partnership administrative adjustment is mailed to the tax matters partner, the tax matters partner may file a petition for a readjustment of the partnership items for such taxable year with—

"(1) the Tax Court,

"(2) the district court of the United States for the district in which the partnership's principal place of business is located, or

"(3) the Claims Court.

"(b) PETITION BY PARTNER OTHER THAN TAX MATTERS PARTNER.—

"(1) IN GENERAL.—If the tax matters partner does not file a readjustment petition under subsection (a) with respect to any final partnership administrative adjustment, any notice partner (and any 5-percent group) may, within 60 days after the close of the 90-day period set forth in subsection (a), file a petition for a readjustment of the partnership items for the taxable year involved with any of the courts described in subsection (a).

"(2) PRIORITY OF THE TAX COURT ACTION.—If more than 1 action is brought under paragraph (1) with respect to any partnership for any partnership taxable year, the first such action brought in the Tax Court shall go forward.

"(3) PRIORITY OUTSIDE THE TAX COURT.—If more than 1 action is brought under paragraph (1) with respect to any partnership for any taxable year but no such action is brought in the Tax Court, the first such action brought shall go forward.

"(4) DISMISSAL OF OTHER ACTIONS.—If an action is brought under paragraph (1) in addition to the action which goes forward under paragraph (2) or (3), such action shall be dismissed.

"(5) TAX MATTERS PARTNER MAY INTERVENE.—The tax matters partner may intervene in any action brought under this subsection.

"(c) PARTNERS TREATED AS PARTIES.—If an action is brought under subsection (a) or (b) with respect to a partnership for any partnership taxable year—

"(1) each person who was a partner in such partnership at any time during such year shall be treated as a party to such action, and

"(2) the court having jurisdiction of such action shall allow each such person to participate in the action.

"(d) PARTNER MUST HAVE INTEREST IN OUTCOME.—

"(1) IN ORDER TO BE PARTY TO ACTION.—Subsection (c) shall not apply to a partner after the day on which—

"(A) the partnership items of such partner for the partnership taxable year became nonpartnership items by reason of 1 or more of the events described in subsection (b) of section 6231, or

"(B) the period within which any tax attributable to such partnership items may be assessed against that partner expired.

"(2) TO FILE PETITION.—No partner may file a readjustment petition under subsection (b) unless such partner would (after the application of paragraph (1) of this subsection) be treated as a party to the proceeding.

"(e) JURISDICTIONAL REQUIREMENT FOR BRINGING ACTION IN DISTRICT COURT OR CLAIMS COURT.—

"(1) IN GENERAL.—A readjustment petition under this section may be filed in a district court of the United States or the Claims Court only if the partner filing the petition deposits

with the Secretary, on or before the day the petition is filed, the amount by which the tax liability of the partner would be increased if the treatment of partnership items on the partner's return were made consistent with the treatment of partnership items on the partnership return, as adjusted by the final partnership administrative adjustment. In the case of a petition filed by a 5-percent group, the requirement of the preceding sentence shall apply to each member of the group. The court may by order provide that the jurisdictional requirements of this paragraph are satisfied where there has been a good faith attempt to satisfy such requirements and any shortfall in the amount required to be deposited is timely corrected.

"(2) Refund on request.—If an action brought in a district court of the United States or in the Claims Court is dismissed by reason of the priority of a Tax Court action under paragraph (2) of subsection (b), the Secretary shall, at the request of the partner who made the deposit, refund the amount deposited under paragraph (1).

"(3) Interest payable.—Any amount deposited under paragraph (1), while deposited, shall not be treated as a payment of tax for purposes of this title (other than chapter 67).

"(f) Scope of Judicial Review.—A court with which a petition is filed in accordance with this section shall have jurisdiction to determine all partnership items of the partnership for the partnership taxable year to which the notice of final partnership administrative adjustment relates and the proper allocation of such items among the partners.

"(g) Determination of Court Reviewable.—Any determination by a court under this section shall have the force and effect of a decision of the Tax Court or a final judgment or decree of the district court or the Claims Court, as the case may be, and shall be reviewable as such. Only the tax matters partner, a notice partner, or a 5-percent group may seek review of a determination by a court under this section.

"(h) Effect of Decision Dismissing Action.—If an action brought under this section is dismissed (other than under paragraph (4) of subsection (b)), the decision of the court dismissing the action shall be considered as its decision that the notice of final partnership administrative adjustment is correct, and an appropriate order shall be entered in the records of the court.

"SEC. 6227. ADMINISTRATIVE ADJUSTMENT REQUESTS.

"(a) General Rule.—A partner may file a request for an administrative adjustment of partnership items for any partnership taxable year at any time which is—

"(1) within 3 years after the later of—

"(A) the date on which the partnership return for such year is filed, or

"(B) the last day for filing the partnership return for such year (determined without regard to extensions), and

"(2) before the mailing to the tax matters partner of a notice of final partnership administrative adjustment with respect to such taxable year.

"(b) REQUESTS BY TAX MATTERS PARTNER ON BEHALF OF PARTNERSHIP.—

"(1) SUBSTITUTED RETURN.—If the tax matters partner—

"(A) files a request for an administrative adjustment, and

"(B) asks that the treatment shown on the request be substituted for the treatment of partnership items on the partnership return to which the request relates,

the Secretary may treat the changes shown on such request as corrections of mathematical or clerical errors appearing on the partnership return.

"(2) REQUESTS NOT TREATED AS SUBSTITUTED RETURNS.—

"(A) IN GENERAL.—If the tax matters partner files an administrative adjustment request on behalf of the partnership which is not treated as a substituted return under paragraph (1), the Secretary may, with respect to all or any part of the requested adjustments—

"(i) without conducting any proceeding, allow or make to all partners the credits or refunds arising from the requested adjustments,

"(ii) conduct a partnership proceeding under this subchapter, or

"(iii) take no action on the request.

"(B) EXCEPTIONS.—Clause (i) of subparagraph (A) shall not apply with respect to a partner after the day on which the partnership items become nonpartnership items by reason of 1 or more of the events described in subsection (b) of section 6231.

"(3) REQUEST MUST SHOW EFFECT ON DISTRIBUTIVE SHARES.—The tax matters partner shall furnish with any administrative adjustment request on behalf of the partnership revised schedules showing the effect of such request on the distributive shares of the partners and such other information as may be required under regulations.

"(c) OTHER REQUESTS.—If any partner files a request for an administrative adjustment (other than a request described in subsection (b)), the Secretary may—

"(1) process the request in the same manner as a claim for credit or refund with respect to items which are not partnership items,

"(2) assess any additional tax that would result from the requested adjustments,

"(3) mail to the partner, under subparagraph (A) of section 6231(b)(1) (relating to items becoming nonpartnership items), a notice that all partnership items of the partner for the partnership taxable year to which such request relates shall be treated as nonpartnership items, or

"(4) conduct a partnership proceeding.

"SEC. 6228. JUDICIAL REVIEW WHERE ADMINISTRATIVE ADJUSTMENT REQUEST IS NOT ALLOWED IN FULL.

"(a) REQUEST ON BEHALF OF PARTNERSHIP.—

"(1) IN GENERAL.—If any part of an administrative adjustment request filed by the tax matters partner under subsection

(b) of section 6227 is not allowed by the Secretary, the tax matters partner may file a petition for an adjustment with respect to the partnership items to which such part of the request relates with—

"(A) the Tax Court,

"(B) the district court of the United States for the district in which the principal place of business of the partnership is located, or

"(C) the Claims Court.

"(2) PERIOD FOR FILING PETITION.—

"(A) IN GENERAL.—A petition may be filed under paragraph (1) with respect to partnership items for a partnership taxable year only—

"(i) after the expiration of 6 months from the date of filing of the request under section 6227, and

"(ii) before the date which is 2 years after the date of such request.

"(B) NO PETITION AFTER NOTICE OF BEGINNING OF ADMINISTRATIVE PROCEEDING.—No petition may be filed under paragraph (1) after the day the Secretary mails to the partnership a notice of the beginning of an administrative proceeding with respect to the partnership taxable year to which such request relates.

"(C) FAILURE BY SECRETARY TO ISSUE TIMELY NOTICE OF ADJUSTMENT.—If the Secretary—

"(i) mails the notice referred to in subparagraph (B) before the expiration of the 2-year period referred to in clause (ii) of subparagraph (A), and

"(ii) fails to mail a notice of final partnership administrative adjustment with respect to the partnership taxable year to which the request relates before the expiration of the period described in section 6229(a) (including any extension by agreement),

subparagraph (B) shall cease to apply with respect to such request, and the 2-year period referred to in clause (ii) of subparagraph (A) shall not expire before the date 6 months after the expiration of the period described in section 6229(a) (including any extension by agreement).

"(D) EXTENSION OF TIME.—The 2-year period described in subparagraph (A)(ii) shall be extended for such period as may be agreed upon in writing between the tax matters partner and the Secretary.

"(3) COORDINATION WITH ADMINISTRATIVE ADJUSTMENT.—

"(A) ADMINISTRATIVE ADJUSTMENT BEFORE FILING OF PETITION.—No petition may be filed under this subsection after the Secretary mails to the tax matters partner a notice of final partnership administrative adjustment for the partnership taxable year to which the request under subsection (b) of section 6227 relates.

"(B) ADMINISTRATIVE ADJUSTMENT AFTER FILING BUT BEFORE HEARING OF PETITION.—If the Secretary mails to the tax matters partner a notice of final partnership administrative adjustment for the partnership taxable year to which the request under section 6227 relates after the filing

of a petition under this subsection but before the hearing of such petition, such petition shall be treated as an action brought under section 6226 with respect to that administrative adjustment, except that subsection (e) of section 6226 shall not apply.

"(C) NOTICE MUST BE BEFORE EXPIRATION OF STATUTE OF LIMITATIONS.—A notice of final partnership administrative adjustment for the partnership taxable year shall be taken into account under subparagraphs (A) and (B) only if such notice is mailed before the expiration of the period prescribed by section 6229 for making assessments of tax attributable to partnership items for such taxable year.

"(4) PARTNERS TREATED AS PARTY TO ACTION.—

"(A) IN GENERAL.—If an action is brought by the tax matters partner under paragraph (1) with respect to any request for an adjustment of a partnership item for any taxable year—

"(i) each person who was a partner in such partnership at any time during the partnership taxable year involved shall be treated as a party to such action, and

"(ii) the court having jurisdiction of such action shall allow each such person to participate in the action.

"(B) PARTNERS MUST HAVE INTEREST IN OUTCOME.—For purposes of subparagraph (A), rules similar to the rules of paragraph (1) of section 6226(d) shall apply.

"(5) SCOPE OF JUDICIAL REVIEW.—Except in the case described in subparagraph (B) of paragraph (3), a court with which a petition is filed in accordance with this subsection shall have jurisdiction to determine only those partnership items to which the part of the request under section 6227 not allowed by the Secretary relates and those items with respect to which the Secretary asserts adjustments as offsets to the adjustments requested by the tax matters partner.

"(6) DETERMINATION OF COURT REVIEWABLE.—Any determination by a court under this subsection shall have the force and effect of a decision of the Tax Court or a final judgment or decree of the district court or the Claims Court, as the case may be, and shall be reviewable as such. Only the tax matters partner, a notice partner, or a 5-percent group may seek review of a determination by a court under this subsection.

"(b) OTHER REQUESTS.—

"(1) NOTICE PROVIDING THAT ITEMS BECOME NONPARTNERSHIP ITEMS.—If the Secretary mails to a partner, under subparagraph (A) of section 6231 (b) (1) (relating to items ceasing to be partnership items), a notice that all partnership items of the partner for the partnership taxable year to which a timely request for administrative adjustment under subsection (c) of section 6227 relates shall be treated as nonpartnership items—

"(A) such request shall be treated as a claim for credit or refund of an overpayment attributable to nonpartnership items, and

"(B) the partner may bring an action under section 7422 with respect to such claim at any time within 2 years of the mailing of such notice.

"(2) OTHER CASES.—

"(A) IN GENERAL.—If the Secretary fails to allow any part of an administrative adjustment request filed under subsection (c) of section 6227 by a partner and paragraph (1) does not apply—

"(i) such partner may, pursuant to section 7422, begin a civil action for refund of any amount due by reason of the adjustments described in such part of the request, and

"(ii) on the beginning of such civil action, the partnership items of such partner for the partnership taxable year to which such part of such request relates shall be treated as nonpartnership items for purposes of this subchapter.

"(B) PERIOD FOR FILING PETITION.—

"(i) IN GENERAL.—An action may be begun under subparagraph (A) with respect to an administrative adjustment request for a partnership taxable year only—

"(I) after the expiration of 6 months from the date of filing of the request under section 6227, and

"(II) before the date which is 2 years after the date of filing of such request.

"(ii) EXTENSION OF TIME.—The 2-year period described in subclause (II) of clause (i) shall be extended for such period as may be agreed upon in writing between the partner and the Secretary.

"(C) ACTION BARRED AFTER PARTNERSHIP PROCEEDING HAS BEGUN.—No petition may be filed under subparagraph (A) with respect to an administrative adjustment request for a partnership taxable year after the Secretary mails to the partnership a notice of the beginning of a partnership proceeding with respect to such year.

"(D) FAILURE BY SECRETARY TO ISSUE TIMELY NOTICE OF ADJUSTMENT.—If the Secretary—

"(i) mails the notice referred to in subparagraph (C) before the expiration of the 2-year period referred to in clause (i) (II) of subparagraph (B), and

"(ii) fails to mail a notice of final partnership administrative adjustment with respect to the partnership taxable year to which the request relates before the expiration of the period described in section 6229(a) (including any extension by agreement),

subparagraph (C) shall cease to apply with respect to such request, and the 2-year period referred to in clause (i) (II) of subparagraph (B) shall not expire before the date 6 months after the expiration of the period described in section 6229(a) (including any extension by agreement).

"SEC. 6229. PERIOD OF LIMITATIONS FOR MAKING ASSESSMENTS.

"(a) GENERAL RULE.—Except as otherwise provided in this section, the period for assessing any tax imposed by subtitle A with respect to any person which is attributable to any partnership item (or affected item) for a partnership taxable year shall not expire before the date which is 3 years after the later of—

"(1) the date on which the partnership return for such taxable year was filed, or

"(2) the last day for filing such return for such year (determined without regard to extensions).

"(b) EXTENSION BY AGREEMENT.—

"(1) IN GENERAL.—The period described in subsection (a) (including an extension period under this subsection) may be extended—

"(A) with respect to any partner, by an agreement entered into by the Secretary and such partner, and

"(B) with respect to all partners, by an agreement entered into by the Secretary and the tax matters partner (or any other person authorized by the partnership in writing to enter into such an agreement),

before the expiration of such period.

"(2) COORDINATION WITH SECTION 6501(c)(4).—Any agreement under section 6501(c)(4) shall apply with respect to the period described in subsection (a) only if the agreement expressly provides that such agreement applies to tax attributable to partnership items.

"(c) SPECIAL RULE IN CASE OF FRAUD, ETC.—

"(1) FALSE RETURN.—If any partner has, with the intent to evade tax, signed or participated directly or indirectly in the preparation of a partnership return which includes a false or fraudulent item—

"(A) in the case of partners so signing or participating in the preparation of the return, any tax imposed by subtitle A which is attributable to any partnership item (or affected item) for the partnership taxable year to which the return relates may be assessed at any time, and

"(B) in the case of all other partners, subsection (a) shall be applied with respect to such return by substituting '6 years' for '3 years.'

"(2) SUBSTANTIAL OMISSION OF INCOME.—If any partnership omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in its return, subsection (a) shall be applied by substituting '6 years' for '3 years'.

"(3) NO RETURN.—In the case of a failure by a partnership to file a return for any taxable year, any tax attributable to a partnership item (or affected item) arising in such year may be assessed at any time.

"(4) RETURN FILED BY SECRETARY.—For purposes of this section, a return executed by the Secretary under subsection (b) of section 6020 on behalf of the partnership shall not be treated as a return of the partnership.

"(d) SUSPENSION WHEN SECRETARY MAKES ADMINISTRATIVE ADJUSTMENT.—If notice of a final partnership administrative adjust-

ment with respect to any taxable year is mailed to the tax matters partner, the running of the period specified in subsection (a) (as modified by other provisions of this section) shall be suspended—

"(1) for the period during which an action may be brought under section 6226 (and, if an action with respect to such administrative adjustment is brought during such period, until the decision of the court in such action becomes final), and

"(2) for 1 year thereafter.

"(e) Unidentified Partner.—If—

"(1) the name, address, and taxpayer identification number of a partner are not furnished on the partnership return for a partnership taxable year, and

"(2)(A) the Secretary, before the expiration of the period otherwise provided under this section with respect to such partner, mails to the tax matters partner the notice specified in paragraph (2) of section 6223(a) with respect to such taxable year, or

"(B) the partner has failed to comply with subsection (b) of section 6222 (relating to notification of inconsistent treatment) with respect to any partnership item for such taxable year,

the period for assessing any tax imposed by subtitle A which is attributable to any partnership item (or affected item) for such taxable year shall not expire with respect to such partner before the date which is 1 year after the date on which the name, address, and taxpayer identification number of such partner are furnished to the Secretary.

"(f) Items Becoming Nonpartnership Items.—If, before the expiration of the period otherwise provided in this section for assessing any tax imposed by subtitle A with respect to the partnership items of a partner for the partnership taxable year, such items become nonpartnership items by reason of 1 or more of the events described in subsection (b) of section 6231, the period for assessing any tax imposed by subtitle A which is attributable to such items (or any item affected by such items) shall not expire before the date which is 1 year after the date on which the items become nonpartnership items.

"SEC. 6230. ADDITIONAL ADMINISTRATIVE PROVISIONS.

"(a) Normal Deficiency Proceedings Do Not Apply to Computational Adjustments.—Subchapter B of this chapter shall not apply to the assessment or collection of any computational adjustment.

"(b) Mathematical and Clerical Errors Appearing on Partnership Return.—

"(1) In general.—Section 6225 shall not apply to any adjustment necessary to correct a mathematical or clerical error (as defined in section 6213(g)(2)) appearing on the partnership return.

"(2) Exception.—Paragraph (1) shall not apply to a partner if, within 60 days after the day on which notice of the correction of the error is mailed to the partner, such partner files with the Secretary a request that the correction not be made.

"(c) Claims Arising Out of Erroneous Computations, Etc.—

"(1) In general.—A partner may file a claim for refund on the grounds that—

"(A) the Secretary erroneously computed any computational adjustment necessary—

"(i) to make the partnership items on the partner's return consistent with the treatment of the partnership items on the partnership return, or

"(ii) to apply to the partner a settlement, a final partnership administrative adjustment, or the decision of a court in an action brought under section 6226 or section 6228(a), or

"(B) the Secretary failed to allow a credit or to make a refund to the partner in the amount of the overpayment attributable to the application to the partner of a settlement, a final partnership administrative adjustment, or the decision of a court in an action brought under section 6226 or section 6228(a) (or erroneously computed the amount of any such credit or refund).

"(2) TIME FOR FILING CLAIM.—

"(A) UNDER PARAGRAPH (1)(A).—Any claim under paragraph (1)(A) shall be filed within 6 months after the day on which the Secretary mails the notice of computational adjustment to the partner.

"(B) UNDER PARAGRAPH (1)(B).—Any claim under paragraph (1)(B) shall be filed within 2 years after whichever of the following days is appropriate:

"(i) the day on which the settlement is entered into,

"(ii) the day on which the period during which an action may be brought under section 6226 with respect to the final partnership administrative adjustment expires, or

"(iii) the day on which the decision of the court becomes final.

"(3) SUIT IF CLAIM NOT ALLOWED.—If any portion of a claim under paragraph (1) is not allowed, the partner may bring suit with respect to such portion within the period specified in subsection (a) of section 6532 (relating to periods of limitations on refund suits).

"(4) NO REVIEW OF SUBSTANTIVE ISSUES.—For purposes of any claim or suit under this subsection, the treatment of partnership items on the partnership return, under the settlement, under the final partnership administrative adjustment, or under the decision of the court (whichever is appropriate) shall be conclusive.

"(d) SPECIAL RULES WITH RESPECT TO CREDITS OR REFUNDS ATTRIBUTABLE TO PARTNERSHIP ITEMS.—

"(1) IN GENERAL.—Except as otherwise provided in this subsection, no credit or refund of an overpayment attributable to a partnership item (or an affected item) for a partnership taxable year shall be allowed or made to any partner after the expiration of the period of limitation prescribed in section 6229 with respect to such partner for assessment of any tax attributable to such item.

"(2) ADMINISTRATIVE ADJUSTMENT REQUEST.—If a request for an administrative adjustment under section 6227 with respect to a partnership item is timely filed, credit or refund of any

overpayment attributable to such partnership item (or an affected item) may be allowed or made at any time before the expiration of the period prescribed in section 6228 for bringing suit with respect to such request.

"(3) CLAIM UNDER SUBSECTION (c).—If a timely claim is filed under subsection (c) for a credit or refund of an overpayment attributable to a partnership item (or affected item), credit or refund of such overpayment may be allowed or made at any time before the expiration of the period specified in section 6532 (relating to periods of limitations on suits) for bringing suit with respect to such claim.

"(4) TIMELY SUIT.—Paragraph (1) shall not apply to any credit or refund of any overpayment attributable to a partnership item (or an item affected by such partnership item) if a partner brings a timely suit with respect to a timely administrative adjustment request under section 6228 or a timely claim under subsection (c) relating to such overpayment.

"(5) OVERPAYMENTS REFUNDED WITHOUT REQUIREMENT THAT PARTNER FILE CLAIM.—In the case of any overpayment by a partner which is attributable to a partnership item (or an affected item) and which may be refunded under this subchapter, to the extent practicable credit or refund of such overpayment shall be allowed or made without any requirement that the partner file a claim therefor.

"(6) SUBCHAPTER B OF CHAPTER 66 NOT APPLICABLE.—Subchapter B of chapter 66 (relating to limitations on credit or refund) shall not apply to any credit or refund of an overpayment attributable to a partnership item (or an affected item).

"(e) TAX MATTERS PARTNER REQUIRED TO FURNISH NAMES OF PARTNERS TO SECRETARY.—If the Secretary mails to any partnership the notice specified in paragraph (1) of section 6223(a) with respect to any partnership taxable year, the tax matters partner shall furnish to the Secretary the name, address, profits interest, and taxpayer identification number of each person who was a partner in such partnership at any time during such taxable year. If the tax matters partner later discovers that the information furnished to the Secretary was incorrect or incomplete, the tax matters partner shall furnish such revised or additional information as may be necessary.

"(f) FAILURE OF TAX MATTERS PARTNER, ETC., TO FULFILL RESPONSIBILITY DOES NOT AFFECT APPLICABILITY OF PROCEEDING.—The failure of the tax matters partner, a pass-thru partner, the representative of a notice group, or any other representative of a partner to provide any notice or perform any act required under this subchapter or under regulations prescribed under this subchapter on behalf of such partner does not affect the applicability of any proceeding or adjustment under this subchapter to such partner.

"(g) DATE DECISION OF COURT BECOMES FINAL.—For purposes of section 6229(d)(1) and section 6230(c)(2)(B), the principles of section 7481(a) shall be applied in determining the date on which a decision of a district court or the Claims Court becomes final.

"(h) EXAMINATION AUTHORITY NOT LIMITED.—Nothing in this subchapter shall be construed as limiting the authority granted to the Secretary under section 7602.

"(i) TIME AND MANNER OF FILING STATEMENTS, MAKING ELECTIONS, ETC.—Except as otherwise provided in this subchapter, each—

"(1) statement,

"(2) election,

"(3) request, and

"(4) furnishing of information,

shall be filed or made at such time, in such manner, and at such place as may be prescribed in regulations.

"(j) PARTNERSHIPS HAVING PRINCIPAL PLACE OF BUSINESS OUTSIDE THE UNITED STATES.—For purposes of sections 6226 and 6228, a principal place of business located outside the United States shall be treated as located in the District of Columbia.

"(k) REGULATIONS.—The Secretary shall prescribe such regulations as may be necessary to carry out the purposes of this subchapter. Any reference in this subchapter to regulations is a reference to regulations prescribed by the Secretary.

"(l) COURT RULES.—Any action brought under any provision of this subchapter shall be conducted in accordance with such rules of practice and procedure as may be prescribed by the Court in which the action is brought.

"SEC. 6231. DEFINITIONS AND SPECIAL RULES.

"(a) DEFINITIONS.—For purposes of this subchapter—

"(1) PARTNERSHIP.—

"(A) IN GENERAL.—Except as provided in subparagraph (B), the term 'partnership' means any partnership required to file a return under section 6031(a).

"(B) EXCEPTION FOR SMALL PARTNERSHIPS.—

"(i) IN GENERAL.—The term 'partnership' shall not include any partnership if—

"(I) such partnership has 10 or fewer partners each of whom is a natural person (other than a nonresident alien) or an estate, and

"(II) each partner's share of each partnership item is the same as his share of every other item.

For purposes of the preceding sentence, a husband and wife (and their estates) shall be treated as 1 partner.

"(ii) ELECTION TO HAVE SUBCHAPTER APPLY.—A partnership (within the meaning of subparagraph (A)) may for any taxable year elect to have clause (i) not apply. Such election shall apply for such taxable year and all subsequent taxable years unless revoked with the consent of the Secretary.

"(2) PARTNER.—The term 'partner' means—

"(A) a partner in the partnership, and

"(B) any other person whose income tax liability under subtitle A is determined in whole or in part by taking into account directly or indirectly partnership items of the partnership.

"(3) PARTNERSHIP ITEM.—The term 'partnership item' means, with respect to a partnership, any item required to be taken into account for the partnership's taxable year under any provision of subtitle A to the extent regulations prescribed by the Secre-

tary provide that, for purposes of this subtitle, such item is more appropriately determined at the partnership level than at the partner level.

"(4) Nonpartnership item.—The term 'nonpartnership item' means an item which is (or is treated as) not a partnership item.

"(5) Affected item.—The term 'affected item' means any item to the extent such item is affected by a partnership item.

"(6) Computational adjustment.—The term 'computational adjustment' means the change in the tax liability of a partner which properly reflects the treatment under this subchapter of a partnership item. All adjustments required to apply the results of a proceeding with respect to a partnership under this subchapter to an indirect partner shall be treated as computational adjustments.

"(7) Tax matters partner.—The tax matters partner of any partnership is—

"(A) the general partner designated as the tax matters partner as provided in regulations, or

"(B) if there is no general partner who has been so designated, the general partner having the largest profits interest in the partnership at the close of the taxable year involved (or, where there is more than 1 such partner, the 1 of such partners whose name would appear first in an alphabetical listing).

If there is no general partner designated under subparagraph (A) and the Secretary determines that it is impracticable to apply subparagraph (B), the partner selected by the Secretary shall be treated as the tax matters partner.

"(8) Notice partner.—The term 'notice partner' means a partner who, at the time in question, would be entitled to notice under subsection (a) of section 6223 (determined without regard to subsections (b)(2) and (e)(1)(B) thereof).

"(9) Pass-thru partner.—The term 'pass-thru partner' means a partnership, estate, trust, electing small business corporation, nominee, or other similar person through whom other persons hold an interest in the partnership with respect to which proceedings under this subchapter are conducted.

"(10) Indirect partner.—The term 'indirect partner' means a person holding an interest in a partnership through 1 or more pass-thru partners.

"(11) 5-percent group.—A 5-percent group is a group of partners who for the partnership taxable year involved had profits interests which aggregated 5 percent or more.

"(12) Husband and wife.—Except to the extent otherwise provided in regulations, a husband and wife who have a joint interest in a partnership shall be treated as 1 person.

"(b) Items Cease To Be Partnership Items in Certain Cases.—

"(1) In general.—For purposes of this subchapter, the partnership items of a partner for a partnership taxable year shall become nonpartnership items as of the date—

"(A) the Secretary mails to such partner a notice that such items shall be treated as nonpartnership items,

"(B) the partner files suit under section 6228(b) after the Secretary fails to allow an administrative adjustment request with respect to any of such items,

"(C) the Secretary enters into a settlement agreement with the partner with respect to such items, or

"(D) such change occurs under subsection (e) of section 6223 (relating to effect of Secretary's failure to provide notice) or under subsection (c) of this section.

"(2) CIRCUMSTANCES IN WHICH NOTICE IS PERMITTED.—The Secretary may mail the notice referred to in subparagraph (A) of paragraph (1) to a partner with respect to partnership items for a partnership taxable year only if—

"(A) such partner—

"(i) has complied with subparagraph (B) of section 6222(b)(1) (relating to notification of inconsistent treatment) with respect to one or more of such items, and

"(ii) has not, as of the date on which the Secretary mails the notice, filed a request for administrative adjustments which would make the partner's treatment of the item or items with respect to which the partner complied with subparagraph (B) of section 6222(b)(1) consistent with the treatment of such item or items on the partnership return, or

"(B)(i) such partner has filed a request under section 6227(b) for administrative adjustment of one or more of such items, and

"(ii) the adjustments requested would not make such partner's treatment of such items consistent with the treatment of such items on the partnership return.

"(3) NOTICE MUST BE MAILED BEFORE BEGINNING OF PARTNERSHIP PROCEEDING.—Any notice to a partner under subparagraph (A) of paragraph (1) with respect to partnership items for a partnership taxable year shall be mailed before the day on which the Secretary mails to the tax matters partner a notice of the beginning of an administrative proceeding at the partnership level with respect to such items.

"(c) REGULATIONS WITH RESPECT TO CERTAIN SPECIAL ENFORCEMENT AREAS.—

"(1) APPLICABILITY OF SUBSECTION.—This subsection applies in the case of—

"(A) assessments under section 6851 (relating to termination assessments of income tax) or section 6861 (relating to jeopardy assessments of income, estate, gift, and certain excise taxes),

"(B) criminal investigations,

"(C) indirect methods of proof of income,

"(D) foreign partnerships, and

"(E) other areas that the Secretary determines by regulation to present special enforcement considerations.

"(2) ITEMS MAY BE TREATED AS NONPARTNERSHIP ITEMS.—To the extent that the Secretary determines and provides by regulations that to treat items as partnership items will interfere with the effective and efficient enforcement of this title in any case

described in paragraph (1), such items shall be treated as nonpartnership items for purposes of this subchapter.

"(3) Special rules.—The Secretary may prescribe by regulation such special rules as the Secretary determines to be necessary to achieve the purposes of this subchapter in any case described in paragraph (1).

"(d) Time for Determining Partner's Profits Interest in Partnership.—

"(1) In general.—For purposes of section 6223(b) (relating to special rules for partnerships with more than 100 partners) and paragraph (11) of subsection (a) (relating to 5-percent group), the interest of a partner in the profits of a partnership for a partnership taxable year shall be determined—

"(A) in the case of a partner whose entire interest in the partnership is liquidated, sold, or exchanged during such partnership taxable year, as of the moment immediately before such liquidation, sale, or exchange, or

"(B) in the case of any other partner, as of the close of the partnership taxable year.

"(2) Indirect partners.—The Secretary shall prescribe regulations consistent with the principles of paragraph (1) to be applied in the case of indirect partners.

"(e) Effect of Judicial Decisions in Certain Proceedings.—

"(1) Determinations at partner level.—No judicial determination with respect to the income tax liability of any partner not conducted under this subchapter shall be a bar to any adjustment in such partner's income tax liability resulting from—

(A) a proceeding with respect to partnership items under this subchapter, or

(B) a proceeding with respect to items which become nonpartnership items—

(i) by reason of 1 or more of the events described in subsection (b), and

(ii) after the appropriate time for including such items in any other proceeding with respect to nonpartnership items.

"(2) Proceedings under section 6228(a).—No judicial determination in any proceeding under subsection (a) of section 6228 with respect to any partnership item shall be a bar to any adjustment in any other partnership item.

"(f) Special Rule for Losses and Credits of Foreign Partnerships.—Except to the extent otherwise provided in regulations, in the case of any partnership the tax matters partner of which resides outside the United States or the books of which are maintained outside the United States, no loss or credit shall be allowable to any partner unless section 6031 is complied with for the partnership's taxable year in which such deduction or credit arose at such time as the Secretary prescribes by regulations.

"SEC. 6232. EXTENSION OF SUBCHAPTER TO WINDFALL PROFIT TAX.

"(a) Inclusion as Partnership Item.—For purposes of applying this subchapter to the tax imposed by chapter 45 (relating to the windfall profit tax), the term 'partnership item' means any item relating to the determination of the tax imposed by chapter 45 to the

extent regulations prescribed by the Secretary provide that, for purposes of this subtitle, such item is more appropriately determined at the partnership level than at the partner level.

"(b) Separate Application.—This subchapter shall be applied separately with respect to—

"(1) partnership items described in subsection (a), and

"(2) partnership items described in section 6231(a)(3).

"(c) Partnership Authorized To Act for Partners.—

"(1) In general.—For purposes of chapter 45 and so much of this subtitle as relates to chapter 45, to the extent and in the manner provided in regulations, a partnership shall be treated as authorized to act for each partner with respect to the determination, assessment, or collection of the tax imposed by chapter 45.

"(2) Partners entitled to 5 percent or more of income may elect out of subsection.—Paragraph (1) shall not apply to any partnership if partners entitled to 5 percent or more of the income of the partnership elect (at the time and in the manner provided in regulations) not to have paragraph (1) apply to the partnership.

"(3) Partner's rights preserved.—Nothing in paragraph (1) shall be construed to take away from any person any right granted to such person by the foregoing sections of this subchapter."

(b) Clerical Amendment.—The table of subchapters for chapter 63 is amended by adding at the end thereof the following:

"Subchapter C. Tax treatment of partnership items."

(c) Technical and Conforming Amendments.—

(1) Section 702 (relating to income and credits of partner) is amended by inserting at the end thereof the following new subsection:

"(d) Cross Reference.—

> ***"For rules relating to procedures for determining the tax treatment of partnership items see subchapter C of chapter 63 (section 6221 and following)."***

(2) Subsection (h) of section 6213 (relating to certain cross references with respect to restrictions on assessment) is amended by inserting at the end thereof the following new paragraph:

> ***"(4) For provision that this subchapter shall not apply in the case of computational adjustments attributable to partnership items, see section 6230(a)."***

(3) Section 6216 (relating to certain cross references with respect to assessments) is amended by inserting at the end thereof the following new paragraph:

> ***"(4) For procedures relating to partnership items, see subchapter C."***

(4) Section 6422 (relating to certain cross references with respect to credits and refunds) is amended by inserting at the end thereof the following new paragraph:

> ***"(15) For special rules in the case of a credit or refund attributable to partnership items, see section 6227 and subsections (c) and (d) of section 6230."***

(5) Subsection (o) of section 6501 (relating to limitations on assessment and collection) is amended to read as follows:

> ***"(o) Special Rules for Partnership Items.—For extension of period in the case of partnership items (as defined in section 6231(a)(3)), see section 6229."***

(6) Section 6504 (relating to certain cross references with respect to limitations on assessments) is amended by inserting at the end thereof the following new paragraph:

> ***"(12) Assessments of tax attributable to partnership items, see section 6229."***

(7) Subsection (g) of section 6511 (relating to limitations on credit or refund) is amended to read as follows:

"(g) Special Rule for Claims With Respect to Partnership Items.—In the case of any tax imposed by subtitle A with respect to any person which is attributable to any partnership item (as defined in section 6231(a)(3)), the provisions of section 6227 and subsections (c) and (d) of section 6230 shall apply in lieu of the provisions of this subchapter."

(8) Subsection (a) of section 6512 (relating to limitations in case of petition to Tax Court) is amended by striking out the period at the end of paragraph (3) and inserting in lieu thereof ", and", and by inserting at the end thereof the following new paragraph:

"(4) As to overpayments attributable to partnership items, in accordance with subchapter C of chapter 63."

(9) Paragraph (2) of section 6512(b) (relating to limit on amount of credit or refund) is amended by striking out "(c), (d), or (g)" each place it appears and inserting in lieu thereof "(c), or (d)".

(10) Section 6515 (relating to certain cross references with respect to limitations on credit or refund) is amended by inserting at the end thereof the following new paragraph:

> ***"(7) Refunds or credits attributable to partnership items, see section 6227 and subsections (c) and (d) of section 6230."***

(11) Section 7422 (relating to civil actions for refund) is amended by redesignating subsection (h) thereof as subsection (i) and by inserting after subsection (g) the following new subsection:

"(h) Special Rule for Actions With Respect to Partnership Items.—No action may be brought for a refund attributable to partnership items (as defined in section 6131(a)(3)) except as provided in section 6228(b) or section 6230(c)."

(12) Section 7451 (relating to fee for filing petition) is amended by adding "or for judicial review under section 6226 or section 6228(a)" at the end thereof.

(13) Subsection (c) of section 7456 (relating to Tax Court Commissioners) is amended by inserting "6226, 6228(a)," before "7428".

(14) Subsection (c) of section 7459 (relating to date of decision) is amended by inserting "or in the case of an action brought under section 6226 or section 6228(a)" after "or under section 7428".

(15) Paragraph (1) of section 7482(b) (relating to venue for review of Tax Court decisions) is amended—

(A) by striking out "or" at the end of subparagraph (D),

(B) by striking out the period at the end of subparagraph (E) and inserting in lieu thereof ", or",

(C) by adding after subparagraph (E) the following new subparagraph:

"(F) in the case of a petition under section 6226 or 6228(a), the principal place of business of the partnership,", and

(D) by inserting ", or the petition under section 6226 or 6228(a)," after "or 7477".

(16) Section 7485 (relating to bond to stay assessment and collection) is amended by redesignating subsection (b) as subsection (c) and inserting after subsection (a) the following new subsection:

"(b) Bond in Case of Appeal of Decision Under Section 6226 or Section 6228(a).—The condition of subsection (a) shall be satisfied if a partner duly files notice of appeal from a decision under section 6226 or 6228(a) and on or before the time the notice of appeal is filed with the Tax Court, a bond in an amount fixed by the Tax Court is filed, and with surety approved by the Tax Court, conditioned upon the payment of deficiencies attributable to the partnership items to which that decision relates as finally determined, together with any interest, additional amounts, or additions to the tax provided by law. Unless otherwise stipulated by the parties, the amount fixed by the Tax Court shall be based upon its estimate of the aggregate of such deficiencies."

(17) Subsection (e) of section 1346 of title 28, United States Code (relating to jurisdiction of district courts with the United States as defendant) is amended by striking out "section 7426 or section" and inserting in lieu thereof "section 6226, 6228(a), 7426, or".

(18)(A) Chapter 91 of title 28, United States Code (relating to Claims Court), is amended by adding at the end thereof the following new section:

"§ 1508. Jurisdiction for certain partnership proceedings

"The Claims Court shall have jurisdiction to hear and to render judgment upon any petition under section 6226 or 6228(a) of the Internal Revenue Code of 1954."

(B) The section analysis of chapter 91 of title 28, United States Code (relating to Claims Court) is amended by adding at the end thereof the following new item:

"1508. Jurisdiction for certain partnership proceedings."

SEC. 403. REQUIREMENT THAT STATEMENT BE FURNISHED TO PARTNER.

(a) General Rule.—Section 6031 (relating to return of partnership income) is amended by adding at the end thereof the following new subsection:

"(b) Copies to Partners.—Each partnership required to file a return under subsection (a) for any partnership taxable year shall (on or before the day on which the return for such taxable year was

filed) furnish to each person who is a partner at any time during such taxable year a copy of such information shown on such return as may be required by regulations."

(b) Conforming Amendment.—Section 6031 is amended by striking out "Every partnership" and inserting in lieu thereof the following:

"(a) General Rule.—Every partnership".

SEC. 404. RETURNS REQUIRED FROM ALL PARTNERSHIPS WITH UNITED STATES PARTNERS.

Except as hereafter provided in regulations prescribed by the Secretary of the Treasury or his delegate, nothing in section 6031 of the Internal Revenue Code of 1954 shall be treated as excluding any partnership from the filing requirements of such section for any taxable year if the income tax liability under subtitle A of such Code of any United States person is determined in whole or in part by taking into account (directly or indirectly) partnership items of such partnership for such taxable year.

SEC. 405. RETURN REQUIREMENT FOR UNITED STATES PERSONS HAVING INTEREST IN FOREIGN PARTNERSHIPS.

(a) In General.—Subpart B of part III of subchapter A of chapter 61 (relating to information concerning transactions with other persons) is amended by inserting after section 6046 the following new section:

"SEC. 6046A. RETURNS AS TO INTERESTS IN FOREIGN PARTNERSHIPS.

"(a) Requirement of Return.—Any United States person, except to the extent otherwise provided by regulations—

"(1) who acquires any interest in a foreign partnership,

"(2) who disposes of any portion of his interest in a foreign partnership, or

"(3) whose proportional interest in a foreign partnership changes substantially,

shall file a return.

"(b) Form and Contents of Return.—Any return required by subsection (a) shall be in such form and set forth such information as the Secretary shall by regulations prescribe.

"(c) Time for Filing Return.—Any return required by subsection (a) shall be filed on or before the 90th day (or on or before such later day as the Secretary may by regulations prescribe) after the day on which the United States person becomes liable to file such return.

"(d) Cross Reference.—

"For provisions relating to penalties for violations of this section, see sections 6679 and 7203."

(b) Penalty.—

Subsection (a) of section 6679 (relating to failure to file returns as to organization or reorganization of foreign corporations and acquisitions of their stock) is amended by striking out "section 6046" and inserting in lieu thereof "section 6046 or 6046A".

(c) Clerical Amendments.—

(1) The table of sections for subpart B of part III of subchapter A of chapter 61 is amended by inserting after the item relating to section 6046 the following new item:

"Sec. 6046A. Returns as to interests in foreign partnerships."

(2) The section heading of section 6679 is amended to read as follows:

"SEC. 6679. FAILURE TO FILE RETURNS WITH RESPECT TO FOREIGN CORPORATIONS OR FOREIGN PARTNERSHIPS."

(3) The table of sections for subchapter B of chapter 68 is amended by striking out the item relating to section 6679 and inserting in lieu thereof the following:

"Sec. 6679. Failure to file returns with respect to foreign corporations or foreign partnerships."

SEC. 406. SPECIAL RULE FOR CERTAIN INTERNATIONAL SATELLITE PARTNERSHIPS.

Subchapter C of chapter 63 of the Internal Revenue Code of 1954 (relating to tax treatment of partnership items), section 6031 of such Code (relating to returns of partnership income), and section 6046A of such Code (relating to returns as to interest in foreign partnerships) shall not apply to the International Telecommunications Satellite Organization, the International Maritime Satellite Organization, and any organization which is a successor of either of such organizations.

SEC. 407. EFFECTIVE DATES.

(a)(1) Except as provided in paragraph (2), the amendments made by sections 402, 403, and 404 shall apply to partnership taxable years beginning after the date of the enactment of this Act.

(2) Section 6232 of the Internal Revenue Code of 1954 shall apply to periods after December 31, 1982.

(3) The amendments made by sections 402, 403, and 404 shall apply to any partnership taxable year (or in the case of section 6232 of such Code, to any period) ending after the date of the enactment of this Act if the partnership, each partner, and each indirect partner requests such application and the Secretary of the Treasury or his delegate consents to such application.

(b) The amendments made by section 405 shall apply with respect to acquisitions or dispositions of, or substantial changes in, interests in foreign partnerships occurring after the date of the enactment of this Act.

TITLE V—AIRPORT AND AIRWAY IMPROVEMENT

SECTION 501. SHORT TITLE.

This title may be cited as the "Airport and Airway Improvement Act of 1982".

SEC. 502. DECLARATION OF POLICY.

(a) IN GENERAL.—The Congress hereby finds and declares that—

(1) the safe operation of the airport and airway system will continue to be the highest aviation priority;

(2) the continuation of airport and airway improvement programs and more effective management and utilization of the Nation's airport and airway system are required to meet the current and projected growth of aviation and the requirements

of interstate commerce, the Postal Service, and the national defense;

(3) this title should be administered in a manner to provide adequate navigation aids and airport facilities, including reliever airports and reliever heliports, for points where scheduled commercial air service is provided;

(4) this title should be administered in a manner consistent with a comprehensive airspace system plan to maximize the use of safety facilities, with highest priority for commercial service airports, including but not limited to, the goal of installing, operating, and maintaining, to the extent possible under available funds and given other safety needs, a precision approach system and a full approach light system for each primary runway, grooving, or friction treatment of all primary and secondary runways, a nonprecision instrument approach for all secondary runways, runway end identifier lights on all runways that do not have an approach light system, electronic or visual vertical guidance on all runways, runway edge lighting and marking, and radar approach coverage for all airport terminal areas;

(5) all airport and airway programs should be administered in a manner consistent with the provisions of sections 102 and 103 of the Federal Aviation Act of 1958, with due regard for the goals expressed therein of fostering competition, preventing unfair methods of competition in air transportation, maintaining essential air transportation, and preventing unjust and discriminatory practices;

(6) reliever airports make an important contribution to the efficient operation of the airport and airway system, and special emphasis should be given to their development;

(7) aviation facilities should be constructed and operated with due regard to minimizing current and projected noise impacts on nearby communities;

(8) the Federal administrative requirements placed upon airport sponsors can be reduced and simplified through the use of a single project application to cover all airport improvement projects contained in the airport's annual expenditure program; and

(9) it is in the national interest to develop in metropolitan areas an integrated system of airports designed to provide expeditious access and maximum safety.

(b) Transportation Planning.—It is declared to be in the national interest to encourage and promote the development of transportation systems embracing various modes of transportation in a manner that will serve the States and local communities efficiently and effectively. To accomplish this objective, the Secretary shall cooperate with State and local officials in the development of airport plans and programs which are formulated on the basis of overall transportation needs and coordinated with other transportation planning with due consideration to comprehensive long-range land-use and access plans and overall social, economic, environmental, system performance, and energy conservation goals and objectives. The process shall be continuing, cooperative, and comprehensive to the degree appropriate based on the complexity of the transportation problems.

SEC. 503. DEFINITIONS.

(a) In General.—As used in this title—

(1) "Airport" means any area of land or water which is used, or intended for use, for the landing and takeoff of aircraft, and any appurtenant areas which are used, or intended for use, for airport buildings or other airport facilities or rights-of-way, together with all airport buildings and facilities located thereon.

(2) "Airport development" means any of the following activities, if undertaken by the sponsor, owner or operator of a public-use airport:

(A) any work involved in constructing, reconstructing, repairing, or improving a public-use airport or portion thereof, including—

(i) the removal, lowering, relocation, and marking and lighting of airport hazards; and

(ii) the preparation of plans and specifications, including field investigations incidental thereto;

(B) any acquisition or installation at or by a public-use airport of—

(i) navigation and other aids (including, but not limited to, precision approach systems) used by aircraft for landing at or taking off from such airport, including any necessary site preparation thereby required;

(ii) safety or security equipment required by the Secretary by rule or regulation for the safety or security of persons and property at such airport, or specifically approved by the Secretary as contributing significantly to the safety or security of persons and property at such airport;

(iii) snow removal equipment;

(iv) aviation-related weather reporting equipment; or

(v) equipment to measure runway surface friction; and

(C) any acquisition of land or of any interest therein, or of any easement through or other interest in airspace, including land for future airport development, which is necessary to permit any airport development described in subparagraph (A) or (B) of this paragraph or to remove, mitigate, prevent, or limit the establishment of airport hazards.

(3) "Airport hazard" means any structure or object of natural growth located on or in the vicinity of a public-use airport, or any use of land near such an airport, which obstructs the airspace required for the flight of aircraft in landing or taking off at such airport or is otherwise hazardous to such landing or taking off of aircraft.

(4) "Airport planning" means planning as defined by such regulations as the Secretary shall prescribe, and includes integrated airport system planning.

(5) "Commercial service airport" means a public airport which is determined by the Secretary to enplane annually 2,500 or more passengers and receive scheduled passenger service of aircraft.

(6) "Government aircraft" means aircraft owned and operated by the United States.

(7) "Integrated airport system planning" means the initial as well as continuing development for planning purposes of information and guidance to determine the extent, type, nature, location, and timing of airport development needed in a specific area to establish a viable, balanced, and integrated system of public-use airports. It includes identification of system needs, development of estimates of systemwide development costs, and the conduct of such studies, surveys, and other planning actions, including those related to airport access, as may be necessary to determine the short-, intermediate-, and long-range aeronautical demands required to be met by a particular system of airports. It also includes the establishment by a State of standards, other than standards for safety of approaches, for airport development at public-use airports which are not primary airports.

(8) "Landing area" means that area used or intended to be used for the landing, takeoff, or surface maneuvering of aircraft.

(9) "Passengers enplaned" means domestic, territorial, and international revenue passenger enplanements in the States in scheduled and nonscheduled service of aircraft in intrastate, interstate, and foreign commerce as shall be determined by the Secretary pursuant to such regulations as the Secretary may prescribe.

(10) "Planning agency" means any planning agency designated by the Secretary which is authorized by the laws of the State or States or political subdivisions concerned to engage in areawide planning for the areas in which assistance under this title is to be used.

(11) "Primary airport" means a commercial service airport which is determined by the Secretary to have .01 percent or more of the total number of passengers enplaned annually at all commercial service airports.

(12) "Project" means a project (or separate projects submitted together) for the accomplishment of airport development or airport planning, including the combined submission of all projects which are to be undertaken at an airport in a fiscal year.

(13) "Project costs" means any costs involved in accomplishing a project.

(14) "Project grant" means a grant of funds by the Secretary to a sponsor for the accomplishment of one or more projects.

(15) "Public agency" means a State or any agency of a State, a municipality or other political subdivision of a State, a tax-supported organization, or an Indian tribe or pueblo.

(16) "Public airport" means any airport which is used or to be used for public purposes, under the control of a public agency, the landing area of which is publicly owned.

(17) "Public-use airport" means—

(A) any public airport,

(B) any privately owned reliever airport, and

(C) any privately owned airport which is determined by the Secretary to enplane annually 2,500 or more passengers and receive scheduled passenger service of aircraft,

which is used or to be used for public purposes.

(18) "Reliever airport" means an airport designated by the Secretary as having the function of relieving congestion at a commercial service airport and providing more general aviation access to the overall community.

(19) "Reliever heliport" means a heliport designated by the Secretary as having the function of relieving congestion at a commercial service airport, by means of diverting potential fixed-wing enplaned passengers to helicopter carriers.

(20) "Secretary" means the Secretary of Transportation.

(21) "Sponsor" means (A) any public agency which, either individually or jointly with one or more other public agencies, submits to the Secretary, in accordance with this title, an application for financial assistance, and (B) any private owner of a public-use airport who submits to the Secretary, in accordance with this title, an application for financial assistance for such airport.

(22) "State" means a State of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Virgin Islands, American Samoa, the Government of the Northern Mariana Islands, the Trust Territory of the Pacific Islands, and Guam.

(23) "Trust Fund" means the Airport and Airway Trust Fund established by section 9502 of the Internal Revenue Code of 1954.

(24) "United States share" means that portion of the project costs of projects for airport development or airport planning approved pursuant to section 509 of this title which is to be paid from funds made available for the purposes of this title.

(b) AMOUNTS MADE AVAILABLE.—Whenever in this title reference is made to the amount made available for a fiscal year under section 505 of this title, such reference shall mean the amount made available for obligation under subsection (a) of section 505 for that fiscal year as reduced or limited by any Act of Congress enacted after the date of enactment of this title.

SEC. 504. NATIONAL AIRPORT AND AIRWAY SYSTEM PLANS.

(a) FORMULATION OF AIRPORT PLAN.—Not later than two years after the date of enactment of this title and every two years thereafter, the Secretary shall publish the status of the existing national airport system plan to provide for the development of public-use airports in the United States. The plan shall include the type and estimated cost of eligible airport development considered by the Secretary to be necessary to provide a safe, efficient, and integrated system of public-use airports to anticipate and meet the needs of civil aeronautics, to meet requirements in support of the national defense as determined by the Secretary of Defense, and to meet identified needs of the Postal Service. Airport development identified by this plan shall not be limited to the requirements of any classes or categories of public-use airports. In reviewing and revising the plan, the Secretary shall consider the needs of all segments of civil aviation, and take into consideration, among other things, the relationship of each airport to (1) the rest of the transportation system in the particular area, (2) the forecasted technological developments in aeronautics, and (3) developments forecasted in other modes of inter-

city transportation. After the date of enactment of this title, the revised national airport system plan shall be known as the national plan of integrated airport systems.

(b) FORMULATION OF AIRWAY PLAN.—(1) The Administrator of the Federal Aviation Administration shall prepare (subject to the requirements of section 506(f) of this title) and submit to the Congress, not later than ninety days after the date of enactment of this title, a national airways system plan. The Administrator shall review, revise, and publish such plan before the beginning of each fiscal year thereafter. The plan shall set forth, for a ten-year period, the research, engineering, and development programs and the facilities and equipment considered by the Administrator necessary for a system of airways, air traffic services, and navigation aids which will meet the forecasted needs of civil aeronautics, meet requirements in support of the national defense as determined by the Secretary of Defense, and provide the highest degree of safety in air commerce. In addition, such plan shall set forth—

(A) for the first two years of the plan, detailed annual estimates of (i) the number, type, location, and cost of acquisition, operation, and maintenance of required facilities and services, (ii) the cost of research, engineering, and development required to improve safety, system capacity, and efficiency, and (iii) manpower levels required for all the activities described in this subparagraph;

(B) for the third, fourth, and fifth years of the plan, estimates of the total cost of each major program for such three-year period, and any additional major research programs, acquisition of systems and facilities, and changes in manpower levels that may be required to meet long-range objectives and that may have significant impact on future funding requirements; and

(C) a ten-year investment plan which considers long-range objectives considered by the Administrator to be necessary to ensure that safety is given the highest priority in providing for a safe and efficient airway system and to meet the current and projected growth of aviation and the requirements of interstate commerce, the Postal Service, and the national defense.

(2) On or before the first day of April of each year the Secretary shall report to the Congress on the operations of the national airways system during the last completed fiscal year. The report shall include a review of the operations of the Federal Aviation Administration, including, but not limited to, a detailed report on programs intended to improve the safety of flight operations and the capacity and efficiency of the national airways system, any significant problems encountered in these programs, a summary of funds committed in each major program area, and a report on amounts appropriated but not expended for such programs.

(c) CONSULTATION WITH FEDERAL AND PUBLIC AGENCIES AND AVIATION COMMUNITY.—In reviewing and revising the national airport system plan, the Secretary shall consult, to the extent feasible and as appropriate, with other Federal and public agencies, and with the aviation community.

(d) CONSULTATION WITH DEPARTMENT OF DEFENSE.—(1) The Department of Defense shall make domestic military airports and air-

port facilities available for civil use to the maximum extent feasible. In advising the Secretary of national defense requirements pursuant to subsection (a) of this section, the Secretary of Defense shall indicate the extent to which domestic military airports and airport facilities will be available for civil use.

(2) Not later than 180 days after the date of enactment of this title, the Comptroller General shall submit to the Congress an evaluation of the feasibility of making domestic military airports and airport facilities available for joint civil and military use to the maximum extent compatible with national defense requirements. With respect to those military airports determined to be most feasible for joint civil and military use, such evaluation shall include an estimate of the costs and the development requirements involved in making such airports available for joint civil and military use.

(3) Not later than 1 year after the date of enactment of this title, the Secretary of Defense and the Secretary of Transportation shall submit to the Congress a plan for making domestic military airports and airport facilities available for joint civil and military use to the maximum extent compatible with national defense requirements. The plan shall recommend public-sector civil sponsors in the case of each joint use proposed in the plan.

SEC. 505. AIRPORT IMPROVEMENT PROGRAM.

(a) AIRPORT DEVELOPMENT AND AIRPORT PLANNING.—In order to maintain a safe and efficient nationwide system of public-use airports to meet the present and future needs of civil aeronautics, the Secretary is authorized to make grants from the Trust Fund for airport development and airport planning by project grants in accordance with the provisions of this title. The aggregate amounts which shall be available after September 30, 1981, to the Secretary for such grants and for grants for airport noise compatibility planning under section 103(b) of the Aviation Safety and Noise Abatement Act of 1979 and for carrying out noise compatibility programs or parts thereof under section 104(c) of such Act shall be $450,000,000 for fiscal year 1982; $1,050,000,000 for the fiscal years ending before October 1, 1983; $1,843,500,000 for the fiscal years ending before October 1, 1984; $2,755,500,000 for the fiscal years ending before October 1, 1985; $3,772,500,000 for the fiscal years ending before October 1, 1986; and $4,789,700,000 for the fiscal years ending before October 1, 1987.

(b) OBLIGATIONAL AUTHORITY.—(1) The Secretary is authorized to incur obligations to make grants from funds made available under subsection (a) of this section, and such authority shall exist with respect to funds available for the making of grants for any fiscal year or part thereof pursuant to subsection (a) immediately after such funds are apportioned pursuant to section 507(a) of this title. No such obligation shall be incurred by the Secretary after September 30, 1987, except that nothing in this section shall preclude the obligation by grant agreement of apportioned funds which remain available pursuant to section 508(a) of this title after such date.

(2) No obligation shall be incurred by the Secretary for airport development at a privately owned public-use airport unless the Secretary receives appropriate assurances that such airport will continue to function as a public-use airport during the economic life (which

in no case shall be less than ten years) of any facility at such airport that was developed with Federal financial assistance under this title.

(c) Noise Abatement Projects To Be Considered as Airport Development for Fiscal Year 1982.—For purposes of amounts apportioned for fiscal year 1982, airport development shall be considered to include any of the following activities, if undertaken by the sponsor, owner, or operator of a public-use airport:

(1) any acquisition or installation of the following items for improving noise compatibility at a public-use airport:

(A) noise suppressing equipment, physical barriers, or landscaping, for the purpose of diminishing the effect of aircraft noise on any area adjacent to such airport; and

(B) land, including land associated with future airport development, or any interest therein, or any easement through or other interest in airspace, necessary to insure that such land is used only for purposes which are compatible with the noise levels attributable to the operation of such airport; and

(2) any project to carry out an approved airport noise compatibility program, or part thereof, approved by the Secretary pursuant to section 104(b) of the Aviation Safety and Noise Abatement Act of 1979.

SEC. 506. AIRWAY IMPROVEMENT PROGRAM.

(a) Airway Facilities and Equipment.—For the purposes of acquiring, establishing, and improving air navigation facilities under section 307(b) of the Federal Aviation Act of 1958 (49 U.S.C. 1348(b)), there is authorized to be appropriated from the Trust Fund for fiscal years beginning after September 30, 1981, aggregate amounts not to exceed $261,000,000 for fiscal year 1982; $986,000,000 for the fiscal years ending before October 1, 1983; $2,379,000,000 for the fiscal years ending before October 1, 1984; $3,786,000,000 for the fiscal years ending before October 1, 1985; $5,163,000,000 for the fiscal years ending before October 1, 1986; and $6,327,000,000 for the fiscal years ending before October 1, 1987. Amounts appropriated under the authorizations in this subsection shall remain available until expended.

(2) The costs of site preparation work associated with acquisition, establishment, or improvement of air navigation facilities by the Secretary pursuant to section 307(b) of the Federal Aviation Act of 1958 shall be charged to appropriated funds available to the Secretary for that purpose pursuant to paragraph (1) of this subsection. Nothing in this title shall preclude the Secretary from providing, in a grant agreement or other agreement with an airport owner or sponsor, for the performance of such site preparation work in connection with airport development, subject to payment or reimbursement for such site preparation work by the Secretary from such appropriated funds.

(b) Research, Engineering and Development, and Demonstrations.—The Secretary is authorized to carry out under section 312 (49 U.S.C. 1353) of the Federal Aviation Act of 1958 such demonstration projects as the Secretary determines necessary in connection with research and development activities under section 312. For

research, engineering and development, and demonstration projects and activities under section 312, there is authorized to be appropriated from the Trust Fund $72,000,000 for fiscal year 1982; $134,000,000 for fiscal year 1983 (of which not more than $16,800,000 is authorized to be appropriated for facilities, engineering and development); $286,000,000 for fiscal year 1984 (of which not more than $24,700,000 is authorized to be appropriated for facilities, engineering and development); $269,000,000 for fiscal year 1985 (of which not more than $23,100,000 is authorized to be appropriated for facilities, engineering and development); $215,000,000 for fiscal year 1986 (of which not more than $22,700,000 is authorized to be appropriated for facilities, engineering and development); and $193,000,000 for fiscal year 1987 (of which not more than $22,000,000 is authorized to be appropriated for facilities, engineering and development). Amounts appropriated under the authorizations in this subsection shall remain available until expended.

(c) OTHER EXPENSES.—(1) The balance of the moneys available in the Trust Fund may be appropriated for (A) costs of services provided under international agreements relating to the joint financing of air navigation services which are assessed against the United States Government, and (B) direct costs incurred by the Secretary to flight check, operate, and maintain air navigation facilities referred to in subsection (a) of this section in a safe and efficient manner.

(2) The amount appropriated from the Trust Fund for the purposes of clauses (A) and (B) of paragraph (1) of this subsection for fiscal year 1982 may not exceed $800,000,000, and for any fiscal year beginning after September 30, 1982, and ending before October 1, 1987, may not exceed the amount made available for purposes of section 505 for that fiscal year multiplied by a factor equal to 2.44 in the case of fiscal year 1983; 1.57 in the case of fiscal year 1984; 1.39 in the case of fiscal year 1985; 1.28 in the case of fiscal year 1986; and 1.34 in the case of fiscal year 1987. The amount authorized to be appropriated from the Trust Fund under this paragraph for any fiscal year shall be reduced by an amount equal to two times the excess, if any, of (A) the portion of the amount authorized to be appropriated under subsection (a) of this section for such fiscal year which was not authorized to be appropriated for any previous fiscal year, over (B) the amount appropriated under such subsection for such fiscal year.

(d) WEATHER SERVICES.—The Secretary is authorized to reimburse the National Oceanic and Atmospheric Administration from the funds authorized in subsection (c) for fiscal years beginning after September 30, 1982, for the cost of providing the Federal Aviation Administration with weather reporting services. Expenditures for the purposes of carrying out this subsection shall be limited to $26,700,000 for fiscal year 1983; $28,569,000 for fiscal year 1984; $30,569,000 for fiscal year 1985; $32,709,000 for fiscal year 1986; and $34,998,000 for fiscal year 1987.

(e) PRESERVATION OF FUNDS AND PRIORITY FOR AIRPORT AND AIRWAY PROGRAMS.—(1) Notwithstanding any other provision of law to the contrary, no amounts may be appropriated from the Trust Fund to carry out any program or activity under the Federal Aviation Act of 1958, except programs or activities referred to in this section.

(2) Amounts equal to the amounts authorized for each fiscal year by section 505 of this title and subsections (a), (b), and (d) and the third sentence of section (c) of this section shall remain available in the Trust Fund until appropriated for the purposes described in such subsections.

(3) No amounts in the Trust Fund may be appropriated for any fiscal year to carry out administrative expenses of the Department of Transportation or of any unit thereof except to the extent authorized by subsection (c) of this section.

(4) No provision of law, except for a statute enacted after the date of enactment of this title which expressly limits the application of this paragraph, shall impair the authority of the Secretary to obligate to an airport by grant agreement in any fiscal year the unobligated balance of amounts which were apportioned in prior fiscal years and which remain available for approved airport development projects pursuant to section 508(a) of this title, in addition to the amounts authorized for that fiscal year by section 505.

(5) No provision of law shall be construed as authorizing the Secretary to obligate or expend any amounts appropriated from the Trust Fund for the purposes described in subsection (c) in any fiscal year after September 30, 1987, unless the provision expressly amends the provisions of and the formulas in subsection (c) of this section.

(f) TRANSMITTAL OF BUDGET ESTIMATES.—Whenever the Administrator of the Federal Aviation Administration submits or transmits any budget estimate, budget request, supplemental budget estimate, or other budget information, legislative recommendation, or comment on legislation to the Secretary, the President of the United States, or to the Office of Management and Budget pertaining to funds authorized in subsection (a) or (b) of this section, it shall concurrently transmit a copy thereof to the Speaker of the House of Representatives, the Committees on Public Works and Transportation and Appropriations of the House of Representatives, the President of the Senate, and the Committees on Commerce, Science, and Transportation and Appropriations of the Senate.

SEC. 507. APPORTIONMENT OF FUNDS.

(a) APPORTIONMENT.—On the first day of each fiscal year for which any amount is authorized to be obligated for the purposes of section 505 of this title, the amount made available for that year under such section and not previously apportioned shall be apportioned by the Secretary as follows:

(1) PRIMARY AIRPORTS.—

(A) To the sponsor of each primary airport, as follows:

(i) $6 for each of the first fifty thousand passengers enplaned at that airport;

(ii) $4 for each of the next fifty thousand passengers enplaned at that airport;

(iii) $2 for each of the next four hundred thousand passengers enplaned at that airport; and

(iv) $0.50 for each additional passenger enplaned at that airport.

(B) In each of the fiscal years 1984 through 1987, the Secretary shall apportion an amount to the sponsor of each primary airport in addition to whatever amount is appor-

tioned to such airport under the formula set forth in subparagraph (A). The additional apportionment shall be calculated by determining the amount such airport is to be apportioned under the formula in subparagraph (A) and then increasing that amount by 10 percent for fiscal year 1984, 20 percent for fiscal year 1985, 25 percent for fiscal year 1986, and 30 percent for fiscal year 1987.

(C) The Secretary shall not apportion less than $200,000 nor more than $12,500,000 under this paragraph to an airport sponsor for any primary airport for any fiscal year.

(D) In no event shall the total amount of all apportionments under this paragraph for any fiscal year exceed 50 percent of the amount authorized to be obligated for such fiscal year for the purposes of section 505 of this title. In any case in which an apportionment would be reduced by the preceding sentence, the Secretary shall for such fiscal year reduce the apportionment to each sponsor of a primary airport under this paragraph proportionately so that such 50 percent amount is achieved.

(E) If any Act of Congress has the effect of limiting or reducing the amount authorized or available to be obligated for any fiscal year for the purposes of section 505 of this title, the total amount of all apportionments under this paragraph for such fiscal year shall not exceed 50 percent of such limited or reduced amount. In any case in which an apportionment would be reduced by the preceding sentence, the Secretary shall for such fiscal year reduce the apportionment to each sponsor of a primary airport under this paragraph proportionately so that such 50 percent amount is achieved.

(2) APPORTIONMENTS TO STATES.—To the States, there shall be apportioned for each of the fiscal years beginning after September 30, 1981, and ending before October 1, 1987, 12 percent of the amount made available under section 505 for such fiscal year, as follows:

(A) INSULAR AREAS.—For airports other than primary airports, one percent of such amounts to Guam, American Samoa, the government of the Northern Mariana Islands, the Trust Territory of the Pacific Islands, and the Virgin Islands.

(B) STATES.—For airports other than primary airports and other than airports described in section 508(d)(3), one-half of the remaining 99 per centum to the States (other than those to which subparagraph (A) of this paragraph applies) in the proportion which the population of each such State bears to the total population of all such States and one-half of the remaining 99 per centum to the States (other than those to which subparagraph (A) of this paragraph applies) in the proportion which the area of each such State bears to the total area of all such States. As used in this paragraph, the term "population" means the population according to the latest decennial census of the United States and the term "area" includes both land and water.

(3) Discretionary Fund.—Any amounts not apportioned under paragraphs (1), (2), and (4) of this subsection shall constitute a discretionary fund to be distributed at the discretion of the Secretary (subject to the limitations set forth in section 508(d) of this title) for such grants for any of the purposes for which funds are made available under section 505 as the Secretary considers most appropriate for carrying out the purposes of this title.

(4) Notwithstanding any other provision of this subsection, for any fiscal year for which funds are made available under section 505 of this title the Secretary may apportion funds for airports in the State of Alaska in the same manner in which funds were apportioned in fiscal year 1980 under section 15(a) of the Airport and Airway Development Act of 1970. In no event shall the total amount apportioned for such airports under this paragraph for any fiscal year be less than the minimum amounts that were required to be apportioned to such airports in fiscal year 1980 under section 15(a)(3)(A) of such Act. In no event shall a primary airport be apportioned less under this paragraph for a fiscal year than it would be apportioned for such fiscal year under paragraph (1) of this subsection. In no event shall the amount of funds apportioned under this paragraph which are expended at any commercial service airport in the State of Alaska during a fiscal year exceed 110 percent of the amount apportioned to such airport for such fiscal year. Nothing in this paragraph shall be construed as prohibiting the Secretary from making additional project grants to airports in the State of Alaska from the discretionary fund established in paragraph (3) of this subsection.

(b) Passengers Enplaned.—For purposes of determining apportionments for any fiscal year under paragraph (1) of subsection (a) of this section, the number of passengers enplaned at an airport shall be based on the number of passengers enplaned at such airport during the preceding calendar year.

SEC. 508. USE OF APPORTIONED AND DISCRETIONARY FUNDS; MISCELLANEOUS CONDITIONS.

(a) Duration of Availability of Apportioned Amounts.—Each amount apportioned under paragraph (1), (2), or (4) of section 507(a) of this title shall be available for obligation under such apportionment during the fiscal year for which it was first authorized to be obligated and the two fiscal years immediately following. Any amount so apportioned which has not been obligated within such time shall be added to the discretionary fund established by section 507(a)(3) of this title.

(b) Transfer of Certain Apportionments of Primary Airports.—(1) Funds apportioned to a sponsor under section 507(a)(1) of this title may be used for any of the purposes for which funds are made available under section 505 at any public-use airport of such sponsor which is in the national plan of integrated airport systems.

(2) A sponsor may enter into an agreement with the Secretary whereby the sponsor waives receipt of all or part of the funds apportioned to it under such section on the condition that the Secretary make the waived amount available for any of the purposes for

which funds are made available under section 505 to the sponsor of another public-use airport which is a part of the same State or geographical area as the airport of the sponsor making the waiver.

(c) STATES.—Funds apportioned to a State under section 507(a)(2) shall be available for any of the purposes for which funds are made available under section 505 to airports described in section 507(a)(2) which are located in such State. Each sponsor of such an airport may apply to the Secretary for grants from funds apportioned to such State.

(d) GENERAL LIMITATIONS.—(1) Not less than 10 percent of the funds made available under section 505 for any fiscal year shall be distributed to reliever airports during such fiscal year.

(2) Not less than 8 percent of the funds made available under section 505 for any fiscal year shall be obligated during such fiscal year (A) for airport noise compatibility planning under section 103(b) of the Aviation Safety and Noise Abatement Act of 1979 and for carrying out noise compatibility programs or parts thereof under section 104(c) of such Act, and (B) in the case of fiscal year 1982, for any of the purposes set forth in section 505(c) of this title.

(3) Not less than 5.5 percent of the funds made available under section 505 for any fiscal year shall be distributed during such fiscal year to—

(A) commercial service airports which are not primary airports,

(B) public airports (other than commercial service airports) which were eligible for Federal assistance from funds apportioned under section 15(a)(3) of the Airport and Airway Development Act of 1970, and to which section 15(a)(3)(A)(I) of such Act applied during fiscal year 1981, and

(C) public airports (other than commercial service airports) which were eligible for Federal assistance from funds apportioned under section 15(a)(3) of the Airport and Airway Development Act of 1970, and to which section 15(a)(3)(A)(II) of such Act applied during fiscal year 1981.

No amounts obligated from the funds apportioned under paragraph (4) of section 507(a) shall be counted as part of the 5.5 percent required to be distributed under this paragraph for each fiscal year.

(4) Not less than one percent of the funds made available under section 505 for any fiscal year shall be distributed to planning agencies for the purpose of integrated airport system planning during such fiscal year.

(5) If the Secretary determines that he will not be able to distribute the amount of funds required to be distributed under paragraph (1), (2), (3), or (4) of this subsection for any fiscal year because the number of qualified applications submitted in compliance with this title is insufficient to meet such amount, the portion of such amount the Secretary determines will not be distributed shall be available for obligation during such fiscal year for other airports and for other purposes authorized by section 505 of this title.

SEC. 509. SUBMISSION AND APPROVAL OF PROJECT GRANT APPLICATIONS.

(a) SUBMISSION.—(1) Subject to the provisions of this subsection, (A) any public agency, or two or more public agencies acting jointly, or (B) any sponsor of a public-use airport, or two or more such spon-

sors acting jointly, may submit to the Secretary a project grant application for one or more projects, in a form and containing such information as the Secretary may prescribe, setting forth the project proposed to be undertaken. No project grant application shall propose airport development or airport planning except in connection with public-use airports included in the current national plan of integrated airport systems prepared pursuant to section 504 of this title. Nothing in this subsection shall authorize the submission of a project grant application by any public agency which is subject to the law of any State if the submission of such application by the public agency is prohibited by the law of that State. All proposed airport development shall be in accordance with standards established or approved by the Secretary, including, but not limited to, standards for site location, airport layout, site preparation, paving, lighting, and safety of approaches.

(2) Notwithstanding any provision of this title, the sponsor of any airport may submit a project-grant application for airport development (including noise compatibility projects) to the Secretary within 180 days after the date of enactment of this title, and the Secretary may incur obligations to fund such projects, in accordance with the provisions of this title, from funds available for obligation pursuant to section 507(a), if—

(A) a project-grant application or preapplication for such project was submitted to the Secretary before September 30, 1980; or

(B) the project was carried out after September 30, 1980, and before the date of enactment of this title.

(b) APPROVAL.—(1) No project grant application may be approved by the Secretary unless the Secretary is satisfied that—

(A) the project is reasonably consistent with plans (existing at the time of approval of the project) of public agencies authorized by the State in which such airport is located to plan for the development of the area surrounding the airport and will contribute to the accomplishment of the purposes of this title;

(B) sufficient funds are available for that portion of the project costs which are not to be paid by the United States under this title;

(C) the project will be completed without undue delay;

(D) the sponsor which submitted the project grant application has legal authority to engage in the project as proposed; and

(E) all project sponsorship requirements prescribed by or under the authority of this title have been or will be met.

(2) No project grant application for airport development may be approved by the Secretary unless the sponsor, a public agency, or the United States or an agency thereof holds good title, satisfactory to the Secretary, to the landing area of the airport or site therefor, or gives assurance satisfactory to the Secretary that good title will be acquired.

(3) No project grant application for airport development may be approved by the Secretary which does not include provision for (A) land required for the installation of approach light systems; (B) touchdown zone and centerline runway lighting; or (C) high intensity runway lighting, when it is determined by the Secretary that any such item is required for the safe and efficient use of the airport by

aircraft, taking into account the type and volume of traffic utilizing the airport.

(4) No project grant application for airport development may be approved unless the Secretary is satisfied that fair consideration has been given to the interest of communities in or near which the project may be located.

(5) It is declared to be national policy that airport development projects authorized pursuant to this title shall provide for the protection and enhancement of the natural resources and the quality of the environment of the Nation. In implementing this policy, the Secretary shall consult with the Secretary of the Interior and the Administrator of the Environmental Protection Agency with regard to any project included in a project grant application involving airport location, a major runway extension, or runway location which may have a significant impact on natural resources including, but not limited to, fish and wildlife, natural, scenic, and recreation assets, water and air quality, and other factors affecting the environment, and shall authorize no such project found to have significant adverse effect unless the Secretary shall render a finding, in writing, following a full and complete review, which shall be a matter of public record, that no feasible and prudent alternative exists and that all reasonable steps have been taken to minimize such adverse effect.

(6)(A) No project grant application for airport development involving the location of an airport, an airport runway, or a major runway extension may be approved by the Secretary unless the sponsor of the project certifies to the Secretary that there has been afforded the opportunity for public hearings for the purpose of considering the economic, social, and environmental effects of the airport or runway location and its consistency with the goals and objectives of such planning as has been carried out by the community.

(B) When hearings are held under subparagraph (A) of this paragraph, the project sponsor shall, when requested by the Secretary, submit a copy of the transcript to the Secretary.

(7)(A) No project grant application for a project involving airport location, a major runway extension, or runway location may be approved unless the Governor of the State in which such project is to be located certifies in writing to the Secretary that there is reasonable assurance that the project will be located, designed, constructed, and operated so as to comply with applicable air and water quality standards. In any case where such standards have not been approved and where applicable air and water quality standards have been promulgated by the Administrator of the Environmental Protection Agency, certification shall be obtained from such Administrator. Notice of certification or refusal to certify shall be provided within sixty days after the project application has been received by the Secretary.

(B) The Secretary shall condition approval of any such project grant application on compliance during construction and operation with applicable air and water quality standards.

(8) Notwithstanding any other provision of law, the Secretary may approve an application for an airport development project (other than an airport development project to which paragraph (7)(A) applies) at an existing airport without requiring the preparation of an

environmental impact statement with respect to noise for such project if—

(A) completion of the project would allow existing aircraft operations at the airport that involve aircraft that do not comply with the noise standards prescribed for "stage 2" aircraft in section 36.1 of title 14, Code of Federal Regulations, to be replaced by aircraft operations involving aircraft that do comply with such standards; and

(B) the project complies with all other statutory and administrative requirements imposed under this title.

(9) In establishing priorities for the distribution of funds available pursuant to section 507 of this title, the Secretary may give priority to approval of projects that are consistent with integrated airport system plans.

(c) STATE STANDARDS.—The Secretary is authorized to approve standards, other than standards for safety of approaches, established by a State for airport development at public-use airports in such State which are not primary airports, and, upon such approval, such State standards shall be the standards applicable to such airports in lieu of any comparable standard established under subsection (a) of this section. State standards approved under this subsection may be revised from time to time, as the State or the Secretary determines necessary, subject to approval of such revisions by the Secretary.

(d) ACCEPTANCE OF CERTIFICATION.—The Secretary is authorized in connection with any project to require a certification from a sponsor that such sponsor will comply with all of the statutory and administrative requirements imposed on such sponsor under this title in connection with such project. Acceptance by the Secretary of a certification from a sponsor may be rescinded by the Secretary at any time. Nothing in this subsection shall affect or discharge any responsibility or obligation of the Secretary under any other Federal law, including, but not limited to, the National Environmental Policy Act of 1969 (42 U.S.C. 4321 et seq.), section 4(f) of the Department of Transportation Act (49 U.S.C. 1652), title VI of the Civil Rights Act of 1964 (42 U.S.C. 2000b), title VIII of the Act of April 11, 1968 (42 U.S.C. 3601 et seq.), and the Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (42 U.S.C. 4601 et seq.).

(e) REQUIREMENT OF NOTICE.—Each sponsor to which funds are apportioned under section 507(a)(1) of this title shall notify the Secretary, by such time and in a form containing such information as the Secretary may prescribe, of the fiscal year in which it intends to apply, by project grant application, for such funds. If a sponsor does not provide such notification, the Secretary may defer approval of any application for such funds until the fiscal year immediately following the fiscal year in which such application is submitted.

SEC. 510. UNITED STATES SHARE OF PROJECT COSTS.

(a) GENERAL PROVISION.—Except as otherwise provided in this title, the United States share of allowable project costs payable on account of any project contained in an approved project grant application submitted in accordance with this title shall be 90 percent of the allowable project costs.

(b) PROJECTS AT CERTAIN PRIMARY AIRPORTS.—In the case of primary airports enplaning 0.25 percent or more of the total number of passengers enplaned annually at all commercial service airports, the United States share of allowable project costs payable on account of any project contained in an approved project grant application shall be 75 per centum of the allowable project costs.

(c) PROJECTS IN PUBLIC LAND STATES.—In the case of any State containing unappropriated and unreserved public lands and nontaxable Indian lands (individual and tribal) exceeding 5 percent of the total area of all lands therein, the United States share under subsection (a) or (b) shall be increased by whichever is the smaller of the following percentages thereof: (1) 25 percent, or (2) a percentage equal to one-half of the percentage that the area of all such lands in that State is of its total area. In no event shall such United States share, as increased by this subsection, exceed the greater of (A) the percentage share determined under subsection (a) or (b) of this section, or (B) the percentage share applying on June 30, 1975, as determined under subsection 17(b) of the Airport and Airway Development Act of 1970.

SEC. 511. PROJECT SPONSORSHIP.

(a) SPONSORSHIP.—As a condition precedent to approval of an airport development project contained in a project grant application submitted under this title, the Secretary shall receive assurances, in writing, satisfactory to the Secretary, that—

(1) the airport to which the project relates will be available for public use on fair and reasonable terms and without unjust discrimination, including the requirement that (A) each air carrier using such airport (whether as a tenant, nontenant, or subtenant of another air carrier tenant) shall be subject to such nondiscriminatory and substantially comparable rates, fees, rentals, and other charges and such nondiscriminatory and substantially comparable rules, regulations, and conditions as are applicable to all such air carriers which make similar use of such airport and which utilize similar facilities, subject to reasonable classifications such as tenants or nontenants, and combined passenger and cargo flights or all cargo flights, and such classification or status as tenant shall not be unreasonably withheld by any airport provided an air carrier assumes obligations substantially similar to those already imposed on tenant air carriers, and (B) each fixed-based operator at any airport shall be subject to the same rates, fees, rentals, and other charges as are uniformly applicable to all other fixed-based operators making the same or similar uses of such airport utilizing the same or similar facilities, and (C) each air carrier using such airport shall have the right to service itself or to use any fixed-base operator that is authorized by the airport or permitted by the airport to serve any air carrier at such airport;

(2) there will be no exclusive right for the use of the airport by any person providing, or intending to provide, aeronautical services to the public. For purposes of this paragraph, the providing of services at an airport by a single fixed-based operator shall not be construed as an exclusive right if it would be unreasonably costly, burdensome, or impractical for more than one

fixed-based operator to provide such services, and if allowing more than one fixed-based operator to provide such services would require the reduction of space leased pursuant to an existing agreement between such single fixed-based operator and such airport;

(3) the airport and all facilities thereon or connected therewith will be suitably operated and maintained, with due regard to climatic and flood conditions;

(4) the aerial approaches to the airport will be adequately cleared and protected by removing, lowering, relocating, marking, or lighting or otherwise mitigating existing airport hazards and by preventing the establishment or creation of future airport hazards;

(5) appropriate action, including the adoption of zoning laws has been or will be taken, to the extent reasonable, to restrict the use of land adjacent to or in the immediate vicinity of the airport to activities and purposes compatible with normal airport operations, including landing and takeoff of aircraft;

(6) all of the facilities of the airport developed with Federal financial assistance and all those usable for landing and takeoff of aircraft will be available to the United States for use by Government aircraft in common with other aircraft at all times without charge, except, if the use by Government aircraft is substantial, charge may be made for a reasonable share, proportional to such use, of the cost of operating and maintaining the facilities used;

(7) the airport operator or owner will furnish without cost to the Federal Government for use in connection with any air traffic control or navigation activities, or weather-reporting and communication activities related to air traffic control, any areas of land or water, or estate therein, or rights in buildings of the sponsor as the Secretary considers necessary or desirable for construction at Federal expense of space or facilities for such purposes;

(8) all project accounts and records will be kept in accordance with a standard system of accounting prescribed by the Secretary after consultation with appropriate public agencies;

(9) the airport operator or owner will maintain a fee and rental structure for the facilities and services being provided the airport users which will make the airport as self-sustaining as possible under the circumstances existing at that particular airport, taking into account such factors as the volume of traffic and economy of collection, except that no part of the Federal share of an airport development or airport planning project for which a grant is made under this title or under the Federal Airport Act or the Airport and Airway Development Act of 1970 shall be included in the rate base in establishing fees, rates, and charges for users of that airport;

(10) the airport operator or owner will submit to the Secretary such annual or special airport financial and operations reports as the Secretary may reasonably request;

(11) the airport and all airport records will be available for inspection by any duly authorized agent of the Secretary upon reasonable request;

(12) all revenues generated by the airport, if it is a public airport, will be expended for the capital or operating costs of the airport, the local airport system, or other local facilities which are owned or operated by the owner or operator of the airport and directly related to the actual transportation of passengers or property: Provided, however, That if covenants or assurances in debt obligations previously issued by the owner or operator of the airport, or provisions in governing statutes controlling the owner or operator's financing, provide for the use of the revenues from any of the airport owner or operator's facilities, including the airport, to support not only the airport but also the airport owner or operator's general debt obligations or other facilities, then this limitation on the use of all other revenues generated by the airport shall not apply; and

(13) the airport operator or owner who receives a grant for the purchase of land for noise compatibility purposes which is conditioned on the disposal of the acquired land at the earliest practicable time will, subject to the retention or reservation of any interest or right therein necessary to insure that such land is used only for purposes which are compatible with the noise levels of the operation of the airport, use its best efforts to so dispose of such land. The proceeds of such dispositions shall be (A) refunded to the United States for the Trust Fund on a basis proportionate to the United States share of the cost of acquisition of such land, or (B) reinvested in an approved project, pursuant to such regulations as the Secretary shall prescribe.

(b) COMPLIANCE.—To insure compliance with this section, the Secretary shall prescribe such project sponsorship requirements, consistent with the terms of this title, as the Secretary considers necessary. Among other steps to insure such compliance, the Secretary is authorized to enter into contracts with public agencies on behalf of the United States. Whenever the Secretary obtains from a sponsor any area of land or water, or estate therein, or rights in buildings of the sponsor and constructs space or facilities thereon at Federal expense, the Secretary is authorized to relieve the sponsor from any contractual obligation entered into under this title, the Airport and Airway Development Act of 1970, or the Federal Airport Act to provide free space in airport buildings to the Federal Government to the extent the Secretary finds that space no longer required for the purposes set forth in paragraph (7) of subsection (a) of this section.

(c) CONSULTATION.—In making a decision to undertake any airport development project under this title, each sponsor of an airport shall undertake reasonable consultations with affected parties using the airport at which such project is proposed.

SEC. 512. GRANT AGREEMENTS.

(a) OFFER AND ACCEPTANCE.—Upon approving a project grant application, the Secretary, on behalf of the United States, shall transmit to the sponsor or sponsors of the application an offer to make a grant for the United States share of allowable project costs. An offer shall be made upon such terms and conditions as the Secretary considers necessary to meet the requirements of this title and any regulations prescribed thereunder. Each offer shall state a definite amount as the maximum obligation of the United States payable

from funds authorized by this title, and shall stipulate the obligations to be assumed by the sponsor or sponsors. In any case where the Secretary approves a project grant application for a project which will not be completed in one fiscal year, the offer shall, upon request of the sponsor, provide for the obligation of funds apportioned or to be apportioned to the sponsor pursuant to section 507(a)(1) of this title for such fiscal years (including future fiscal years) as may be necessary to pay the United States share of the cost of such project. If and when an offer is accepted in writing by the sponsor, the offer and acceptance shall comprise an agreement constituting an obligation of the United States and of the sponsor. Unless and until an agreement has been executed, the United States may not pay, nor be obligated to pay, any portion of the costs which have been or may be incurred.

(b) MAXIMUM OBLIGATION OF THE UNITED STATES.—When an offer is accepted in writing by a sponsor, the amount stated in the offer as the maximum obligation of the United States may not be increased, except that—

(1) in the case of any project for airport development (other than a project for land acquisition), the maximum obligation of the United States may be increased by not more than 10 percent; and

(2) in the case of any acquisition of land or interests in land, the maximum obligation of the United States may be increased by an amount not to exceed 50 percent of the total increase in allowable project costs attributable to such acquisition in land or interests therein, based upon current credible appraisals.

(c) Notwithstanding any other provision of law, in the case of grants made under the Airport and Airway Development Act of 1970 the maximum obligation of the United States may be increased by not more than 10 percent, and any such increase may be paid for only from funds recovered by the United States from other grants made under that Act.

SEC. 513. PROJECT COSTS.

(a) ALLOWABLE PROJECT COSTS.—Except as provided in section 514 of this title, the United States may not pay, or be obligated to pay, from amounts appropriated to carry out the provisions of this title, any portion of a project cost incurred in carrying out a project for airport development or airport planning unless the Secretary has first determined that the cost is allowable. A project cost is allowable if—

(1) it was a necessary cost incurred in accomplishing an approved project in conformity with the terms and conditions of the grant agreement entered into in connection with the project, including any costs incurred by a recipient in connection with any audit required by the Secretary pursuant to section 518(b) of this title;

(2) it was incurred subsequent to the execution of the grant agreement with respect to the project, and in connection with airport development or airport planning accomplished under the project after the execution of the agreement. However, the allowable costs of a project for airport development may include any necessary costs of formulating the project (including the

costs of field surveys and the preparation of plans and specifications, the acquisition of land or interests therein or easements through or other interests in airspace, and any necessary administrative or other incidental costs incurred by the sponsor specifically in connection with the accomplishment of the project for airport development, which would not have been incurred otherwise) which were incurred prior to the execution of the grant agreement and subsequent to May 13, 1946, and the allowable costs of a project for airport planning may include any necessary and direct costs associated with developing the project work scope which were incurred subsequent to May 13, 1946;

(3) in the opinion of the Secretary it is reasonable in amount, and if the Secretary determines that a project cost is unreasonable in amount, the Secretary may allow as an allowable project cost only so much of such project cost as the Secretary determines to be reasonable, except that in no event may the Secretary allow project costs in excess of the definite amount stated in the grant agreement except to the extent authorized by section 512(b); and

(4) it has not been incurred in any project for airport planning or airport development for which Federal assistance has been granted.

The Secretary is authorized to prescribe such regulations, including regulations with respect to the auditing of project costs, as the Secretary considers necessary to accomplish the purposes of this section.

(b) TERMINAL DEVELOPMENT.—(1) Notwithstanding any other provision of this title, upon certification by the sponsor of any commercial service airport that such airport has, on the date of submittal of the project grant application, all the safety equipment required for certification of such airport under section 612 of the Federal Aviation Act of 1958 and all the security equipment required by rule or regulation, and has provided for access to the passenger enplaning and deplaning area of such airport to passengers enplaning or deplaning from aircraft other than air carrier aircraft, the Secretary may approve, as allowable project costs of a project for airport development at such airport, terminal development (including multimodal terminal development) in nonrevenue-producing public-use areas if such project cost is directly related to the movement of passengers and baggage in air commerce within the boundaries of the airport, including, but not limited to, vehicles for the movement of passengers between terminal facilities or between terminal facilities and aircraft.

(2) Not more than the greater of (A) $200,000, or (B) 60 percent of the sums apportioned under section 507(a)(1) of this title to the sponsor of a primary airport for any fiscal year may be obligated for project costs allowable under paragraph (1) of this subsection. Not more than $200,000 of the sums to be distributed at the discretion of the Secretary under section 507(a)(3) for any fiscal year may be used by the sponsor of a commercial service airport which is not a primary airport for project costs allowable under paragraph (1) of this subsection.

(3) Not more than $25,000,000 may be obligated for project costs allowable under paragraph (1) of this subsection in any fiscal year

at commercial service airports which were not eligible for assistance for terminal development during the fiscal year ending September 30, 1980, under section 20(b) of the Airport and Airway Development Act of 1970.

(4) Sums apportioned under section 507(a) and made available to the sponsor of an air carrier airport (within the meaning of section 11(1) of the Airport and Airway Development Act of 1970, as in effect immediately before the date of enactment of this paragraph) at which terminal development was carried out on or after July 1, 1970, and before July 12, 1976, shall be available, subject to the limitations contained in paragraph (2) of this subsection, for the immediate retirement of the principal of bonds or other evidences of indebtedness the proceeds of which were used for that part of the terminal development at such airport the cost of which would be allowable under paragraph (1) of this subsection if incurred after the effective date of this paragraph, subject to the following conditions:

(A) That such sponsor submit the certification required under paragraph (1) of this subsection.

(B) That the Secretary determine that no project for airport development at such airport outside the terminal area will be deferred if such sums are used for such retirement.

(C) That no funds available for airport development under this title will be obligated for any project for additional terminal development at such airport for a period of three years beginning on the date any such sums are used for such retirement.

(5) Notwithstanding any other provisions of this title, the United States share of project costs allowable under paragraph (1) of this subsection shall not exceed 50 percent.

(6) The Secretary shall approve project costs allowable under paragraph (1) of this subsection under such terms and conditions as may be necessary to protect the interests of the United States.

(c) COSTS NOT ALLOWED.—Except as provided in subsection (b) of this section, the following are not allowable project costs: (1) the cost of construction of that part of an airport development project intended for use as a public parking facility for passenger automobiles; or (2) the cost of construction, alteration, or repair of a hangar or of any part of an airport building except such of those buildings or parts of buildings intended to house facilities or activities directly related to the safety of persons at the airport.

SEC. 514. PAYMENTS UNDER GRANT AGREEMENTS.

The Secretary, after consultation with the sponsor with which a project grant agreement has been entered into, may determine the times and amounts in which payments shall be made under the terms of such agreement. Payments in an aggregate amount not to exceed 90 percent of the United States share of the total estimated allowable project costs may be made from time to time in advance of accomplishment of the airport project to which the payments relate, if the sponsor certifies to the Secretary that the aggregate expenditures to be made from the advance payments will not at any time exceed the cost of the airport development work which has been performed up to that time. If the Secretary determines that the aggregate amount of payments made under a project grant agreement at any time exceeds the United States share of the total allowable *project costs, the United States shall be entitled to recover the excess. If the Secretary finds that any airport development to which the advance payments relate has not been accomplished within a reasonable time or the project is not completed, the United States may recover any part of the advance payment for which the United States received no benefit. Payments under a project grant agreement shall be made to the official or depository authorized by law to receive public funds and designated by the sponsor.*

SEC. 515. PERFORMANCE OF CONSTRUCTION WORK.

(a) Regulations.—The construction work on any project for airport development contained in an approved project grant application submitted in accordance with this title shall be subject to inspection and approval by the Secretary and shall be in accordance with regulations prescribed by the Secretary. Such regulations shall require such cost and progress reporting by the sponsor or sponsors of such project as the Secretary shall deem necessary. No such regulation shall have the effect of altering any contract in connection with any project entered into without actual notice of the regulation.

(b) Minimum Rates of Wages.—All contracts in excess of $2,000 for work on projects for airport development approved under this title which involve labor shall contain provisions establishing minimum rates of wages, to be predetermined by the Secretary of Labor, in accordance with the Davis-Bacon Act, as amended (40 U.S.C. 276a—276a-5), which contractors shall pay to skilled and unskilled labor, and such minimum rates shall be stated in the invitation for bids and shall be included in proposals or bids for the work.

(c) Veterans Preference.—All contracts for work under project grants for airport development approved under this title which involve labor shall contain such provisions as are necessary to insure that, in the employment of labor (except in executive, administrative, and supervisory positions), preference shall be given to veterans of the Vietnam era and disabled veterans. However, this preference shall apply only where the individuals are available and qualified to perform the work to which the employment relates. For the purposes of this subsection—

(1) a Vietnam-era veteran is an individual who served on active duty as defined by section 101(21) of title 38 of the United States Code in the Armed Forces for a period of more than 180 consecutive days any part of which occurred during the period beginning August 5, 1964, and ending May 7, 1975, and who was separated from the Armed Forces under honorable conditions; and

(2) a disabled veteran is an individual described in section 2108(2) of title 5 of the United States Code.

SEC. 516. USE OF GOVERNMENT-OWNED LANDS.

(a) Requests for Use.—Subject to the provisions of subsection (c) of this section, whenever the Secretary determines that use of any lands owned or controlled by the United States is reasonably necessary for carrying out a project under this title at a public airport, or for the operation of any public airport, including lands reasonably necessary to meet future development of an airport in accordance with the national plan of integrated airport systems, the Secretary

shall file with the head of the department or agency having control of the lands a request that the necessary property interests therein be conveyed to the public agency sponsoring the project in question or owning or controlling the airport. The property interest may consist of the title to, or any other interest in, land or any easement through or other interest in airspace.

(b) MAKING OF CONVEYANCES.—Upon receipt of a request from the Secretary under this section, the head of the department or agency having control of the lands in question shall determine whether the requested conveyance is inconsistent with the needs of the department or agency, and shall notify the Secretary of the determination within a period of four months after receipt of the Secretary's request. If the department or agency head determines that the requested conveyance is not inconsistent with the needs of that department or agency, the department or agency head is hereby authorized and directed, with the approval of the Attorney General of the United States, and without any expense to the United States, to perform any acts and to execute any instruments necessary to make the conveyance requested. A conveyance may be made only on the condition that, at the option of the Secretary, the property interest conveyed shall revert to the United States in the event that the lands in question are not developed for airport purposes or used in a manner consistent with the terms of the conveyance. If only a part of the property interest conveyed is not developed for airport purposes, or used in a manner consistent with the terms of the conveyance, only that particular part shall, at the option of the Secretary, revert to the United States.

(c) EXEMPTION OF CERTAIN LANDS.—Unless otherwise specifically provided by law, the provisions of subsections (a) and (b) of this section shall not apply with respect to lands owned or controlled by the United States within any national park, national monument, national recreation area, or similar area under the administration of the National Park Service; within any unit of the National Wildlife Refuge System or similar area under the jurisdiction of the United States Fish and Wildlife Service; or within any national forest or Indian reservation.

SEC. 517. FALSE STATEMENTS.

Any officer, agent, or employee of the United States, or any officer, agent, or employee of any public agency, or any person, association, firm, or corporation who, with intent to defraud the United States—

(1) knowingly makes any false statement, false representation, or false report as to the character, quality, quantity, or cost of the material used or to be used, or the quantity or quality of the work performed or to be performed, or the costs thereof, in connection with the submission of plans, maps, specifications, contracts, or estimates of project costs for any project submitted to the Secretary for approval under this title;

(2) knowingly makes any false statement, false representation, or false report or claim for work or materials for any project approved by the Secretary under this title; or

(3) knowingly makes any false statement or false representation in any report or certification required to be made under this title;

shall, upon conviction thereof, be punished by imprisonment for not to exceed five years or by a fine of not to exceed $10,000, or by both.

SEC. 518. ACCESS TO RECORDS.

(a) RECORDKEEPING REQUIREMENTS.—Each recipient of a grant under this title shall keep such records as the Secretary may prescribe, including records which fully disclose the amount and the disposition by the recipient of the proceeds of the grant, the total cost of the plan or program in connection with which the grant is given or used, and the amount and nature of that portion of the cost of the plan or program supplied by other sources, and such other records as will facilitate an effective audit. The Secretary shall annually review the reporting and recordkeeping requirements under this title to insure that such requirements are kept to the minimum level necessary for the proper administration of this title.

(b) AUDIT AND EXAMINATION.—The Secretary and the Comptroller General of the United States, or any of their duly authorized representatives, shall have access for the purpose of audit and examination to any books, documents, papers, and records of the recipient that are pertinent to grants received under this title. The Secretary may require, as a condition to receipt of a grant under this title, that an appropriate audit be conducted by a recipient.

(c) AUDIT REPORTS.—In any case in which an independent audit is made of the accounts of a recipient of a grant under this title relating to the disposition of the proceeds of such grant or relating to the plan or program in connection with which the grant was given or used, the recipient shall file a certified copy of such audit with the Comptroller General of the United States not later than six months following the close of the fiscal year for which the audit was made. On or before April 15 of each year the Comptroller General shall report to the Congress describing the results of each audit conducted or reviewed by him under this section during the preceding fiscal year. The Comptroller General shall prescribe such regulations as are deemed necessary to carry out the provisions of this subsection.

(d) WITHHOLDING INFORMATION.—Nothing in this section shall authorize the withholding of information by the Secretary or the Comptroller General of the United States, or any officer or employee under the control of either of them, from the duly authorized committees of the Congress.

SEC. 519. GENERAL POWERS.

The Secretary is empowered to perform such acts, to conduct such investigations and public hearings, to issue and amend such orders, and to make and amend such regulations and procedures, pursuant to and consistent with the provisions of this title, as the Secretary considers necessary to carry out the provisions of, and to exercise and perform the Secretary's powers and duties, under this title.

SEC. 520. CIVIL RIGHTS.

The Secretary shall take affirmative action to assure that no person shall, on the grounds of race, creed, color, national origin, or sex, be excluded from participating in any activity conducted with funds received from any grant made under this title. The Secretary shall promulgate such rules as the Secretary deems necessary to *carry out the purposes of this section and may enforce this section, and any rules promulgated under this section, through agency and department provisions and rules which shall be similar to those established and in effect under title VI of the Civil Rights Act of 1964. The provisions of this section shall be considered to be in addition to and not in lieu of the provisions of title VI of the Civil Rights Act of 1964.*

SEC. 521. REPORTS TO CONGRESS.

On or before the first day of April of each year the Secretary shall make a report to the Congress describing his operations under this title during the preceding fiscal-year. The report shall include a detailed statement of the airport development accomplished, the status of each project undertaken, the allocation of appropriations, and an itemized statement of expenditures and receipts.

SEC. 522. REPORT ON ABILITY OF AIRPORTS TO FINANCE AIRPORT DEVELOPMENT NEEDS.

(a) SUBMISSION TO CONGRESS.—Not later than 1 year after the date of enactment of this title, the Secretary shall submit to the Congress a report on whether, and to what extent, those airports which have the ability to finance their capital and operating needs without Federal assistance should be made ineligible to receive Federal assistance for airport development and airport planning under this title.

(b) CONSIDERATIONS.—The study shall consider, among other things: (1) what effect, if any, making such airports ineligible for such Federal assistance would have on the national airport system; (2) whether airports which are made ineligible for assistance, or voluntarily withdraw from the program, should be permitted to collect a passenger facility charge; (3) how such a passenger facility charge could be collected in order to minimize any cost and inconvenience for passengers, airports, and air carriers; (4) the extent to which such a program would permit a reduction in Federal taxes on air transportation; (5) whether the net effect of such a program would lower or increase the cost of air transportation to passengers on our Nation's air carriers; and (6) whether the Congress should implement such a program prior to the expiration of this title.

(c) CONSULTATION.—In conducting the study, the Secretary shall consult with airport operators, air carriers, and representatives of any other groups which may be substantially affected by such a program.

SEC. 523. REPEALS; EFFECTIVE DATE; SAVING PROVISIONS; AND SEPARABILITY.

(a) REPEAL.—Sections 1 through 30 of the Airport and Airway Development Act of 1970 (49 U.S.C. 1701–1730) are repealed on the date of enactment of this title.

(b) EFFECTIVE DATE.—This title and the amendments made by this title shall take effect on the date of enactment of this title.

(c) SAVING PROVISIONS.—(1) All orders, determinations, rules, regulations, permits, contracts, certificates, licenses, grants, rights, and privileges which have been issued, made, granted, or allowed to become effective by the President, the Secretary, or any court of competent jurisdiction or any provision of the Airport and Airway Development Act of 1970 or the Federal Airport Act which are in effect

at the time this title takes effect, are continued in effect according to their terms until modified, terminated, superseded, set aside, or repealed by the Secretary or by any court of competent jurisdiction, or by operation of law.

(2) Notwithstanding any other provision of this title, amounts apportioned before October 1, 1981, pursuant to section 15(a)(3) of the Airport and Airway Development Act of 1970, which have not been obligated by grant agreement before that date, shall remain available for obligation, for the duration of time specified in section 15(a)(5) of that Act, in accordance with the provisions of that Act (other than the second sentence of section 14(b)(2)), to the same extent as though that Act had not been repealed.

(d) SEPARABILITY.—If any provision of this title or the application thereof to any person or circumstance is held invalid, the remainder of the title and the application of the provision to other persons or circumstances is not affected thereby.

SEC. 524. MISCELLANEOUS AMENDMENTS.

(a)(1) Section 308(a) of the Federal Aviation Act of 1958 (49 U.S.C. 1349(a)) is amended by adding at the end thereof the following new sentence: "For purposes of the preceding sentence, the providing of services at an airport by a single fixed-based operator shall not be construed as an exclusive right if it would be unreasonably costly, burdensome, or impractical for more than one fixed-based operator to provide such services, and if allowing more than one fixed-based operator to provide such services would require the reduction of space leased pursuant to an existing agreement between such single fixed-based operator and such airport.".

(2) Section 313(c) of the Federal Aviation Act of 1958 (49 U.S.C. 1354(c)) is amended by inserting "the Airport and Airway Improvement Act of 1982," after "this Act," the first place it appears.

(3) Section 1109(e) of the Federal Aviation Act of 1958 (49 U.S.C. 1509(e)) is amended by striking out "Airport and Airway Development Act of 1970" and inserting in lieu thereof "Airport and Airway Improvement Act of 1982".

(b) The Aviation Safety and Noise Abatement Act of 1979 is amended as follows:

(1) Section 101(1) is amended to read as follows:

> *"(1) the term 'airport' means any public-use airport (as defined by section 503(17) of the Airport and Airway Improvement Act of 1982);".*

(2) Section 101(2) is amended to read as follows:

> *"(2) the term 'airport operator' means, in the case of an airport serving air carriers certificated by the Civil Aeronautics Board, any person holding a valid certificate issued pursuant to section 612 of the Federal Aviation Act of 1958 (49 U.S.C. 1432) to operate an airport, and, in the case of any other airport, the person operating such airport; and".*

(3) Section 103(b) is amended to read as follows:

"(b)(1) The Secretary is authorized to incur obligations to make grants from funds made available under section 505 of the Airport and Airway Improvement Act of 1982 for airport noise compatibility planning to sponsors of airports. The United States share of any airport noise compatibility planning grant under this section shall be

that percent for which a project for airport development at that airport would be eligible under section 510 of the Airport and Airway Improvement Act of 1982.

"(2) For purposes of this Act, the term 'airport noise compatibility planning' means the development for planning purposes of information necessary to prepare and submit (A) the noise exposure map and related information pursuant to subsection (a) of this section, including any cost associated with obtaining such information, or (B) a noise compatibility program for submission pursuant to section 104 of this Act.".

(4) Section 104(c)(1) is amended by striking out "subsection (e) of this section" in the first sentence and inserting in lieu thereof "section 505 of the Airport and Airway Improvement Act of 1982". The last sentence of section 104(c)(1) is amended to read as follows: "All of the provisions of the Airport and Airway Improvement Act of 1982 applicable to project grants made under section 505 of that Act (except section 510 of that Act relating to United States share of project costs) shall be applicable to any grant made under this Act, unless the Secretary determines that any provision of such Act of 1982 is inconsistent with, or unnecessary to carry out, the purposes of this Act.".

(5) Section 108 is amended by striking out "(1) airport noise compatibility planning carried out with grants made under section 13 of the Airport and Airway Development Act of 1970, and (2)" and inserting in lieu thereof "airport noise compatibility planning and".

(c) Section 13(g)(1) of the Surplus Property Act of 1944 (50 App. U.S.C. 1622(g)(1)) is amended by striking out "Airport and Airway Development Act of 1970" and inserting in lieu thereof "Airport and Airway Improvement Act of 1982".

(d) Section 24 of the Airport and Airway Development Act Amendments of 1976 (49 U.S.C. 1356a) is amended by striking out subsection (c) and inserting in lieu thereof the following:

"(c)(1) There is authorized to be appropriated out of the Airport and Airway Trust Fund for amounts expended before the date specified in paragraph (2) of this subsection not to exceed $15,000,000. No such amounts shall be appropriated prior to September 30, 1981.

"(2) No compensation shall be paid by the Secretary of Transportation under this section for amounts expended after the date which is 180 days after the date of enactment of the International Air Transportation Competition Act of 1979.".

(e) Section 31 of the Airport and Airway Development Act of 1970 is amended by striking out "this title" and inserting in lieu thereof "the Airport and Airway Improvement Act of 1982", by inserting "under such Act" after "airport development project", and by inserting "(as defined by section 11(8) of the Airport and Airway Development Act of 1970, as in effect on the date of enactment of this section)" after "general aviation airport".

(f) The last sentence of section 612(b) of the Federal Aviation Act of 1958 (49 U.S.C. 1432(b)) is amended by inserting "(1)" immediately after the words "relating to" and by inserting the following immediately before the period at the end thereof: "and (2) such grooving or other friction treatment for primary and secondary runways as the Secretary determines to be necessary".

SEC. 525. SAFETY CERTIFICATION OF AIRPORTS.

(a) Section 612(a) of the Federal Aviation Act of 1958 (49 U.S.C. 1432(a)) is amended to read as follows:

"POWER TO ISSUE

"SEC. 612. (a) The Administrator is empowered to issue airport operating certificates to, and establish minimum safety standards for the operation of, airports that serve any scheduled or unscheduled passenger operation of air carrier aircraft designed for more than 30 passenger seats.".

(b) Section 612(b) of such Act (49 U.S.C. 1432(b)) is amended by striking out "serving air carriers certificated by the Civil Aeronautics Board" in the first sentence and inserting in lieu thereof "which is described in subsection (a) and which is required by the Administrator, by rule, to be certificated".

(c) Section 612(c) of such Act (49 U.S.C. 1432(c)) is amended by striking out "air carrier airport enplaning annually less than one-quarter of 1 percent of the total number of passengers enplaned at all air carriers airports" and inserting in lieu thereof "airport described in subsection (a)(1) enplaning annually less than one-quarter of 1 percent of the total number of passengers enplaned at all airports described in subsection (a)(1)".

(d) Section 610(a)(8) of such Act (49 U.S.C. 1430(a)(8)) is amended to read as follows:

> *"(8) For any person to operate an airport without an airport operating certificate required by the Administrator pursuant to section 612, or in violation of the terms of any such certificate; and".*

SEC. 526. CONTRACTING AUTHORITY.

In the powers granted under section 519 of this title, the Secretary, in entering into a contract or other agreement with any State or political subdivision thereof for the purpose of permitting such State or subdivision to operate any airport facility within such State or subdivision shall insure that such contract or agreement contain, among others, a provision relieving the United States of any and all liability for the payment of any claim or other obligation arising out of or in connection with acts or omissions of employees of such State or political subdivision in the operation of any such airport facility.

SEC. 527. STUDY OF AIRPORT ACCESS.

(a) The Secretary shall appoint a task force, as provided in subsection (b), to study the problems of allocating the use of airport facilities and airspace (including, but not limited to, gate facilities, landing facilities, airspace slots, and ticketing and terminal space) among persons using or seeking to use such facilities. The task force shall make a study of present methods of allocating the use of airport facilities and airspace, and, if such action is determined to be appropriate, shall make recommendations for improving those methods and for resolving disputes with respect to the use of such facilities. The task force shall report its findings and recommendations to the chairman of the Committee on Public Works and Transportation of the House of Representatives and the chairman of the Com-

mittee on Commerce, Science, and Transportation of the Senate not later than one hundred and twenty days after the task force first meets under subsection (c).

(b) The task force shall consist of the Chairman of the Civil Aeronautics Board, who shall serve as chairman of the task force, and individuals appointed by the Secretary of Transportation not later than sixty days after the date of enactment of this title, including, but not limited to, a representative of each of the following:

(1) the Department of Transportation;

(2) the Department of Justice;

(3) States;

(4) owners and operators of airports, including those owners and operators of airports which do not restrict access, but which provide service to airports where access is currently restricted or is expected to be restricted in the future;

(5) trunk air carriers;

(6) regional air carriers (other than commuter air carriers);

(7) charter air carriers;

(8) commuter air carriers;

(9) all-cargo air carriers;

(10) general aviation;

(11) financial institutions with an interest in the aviation industry; and

(12) aviation consumer groups.

(c) The task force shall meet, at the direction of the chairman, not later than thirty days after all its members have been appointed under subsection (b), and at such other times as may be necessary to complete the study required by this section.

(d) The Secretary shall provide such staff and support services as may be necessary to assist the task force in completing the report required by this section.

SEC. 528. PART-TIME OPERATION OF FLIGHT SERVICE STATIONS.

(a) Beginning on the date of enactment of this title, the Secretary shall not close or operate on a part-time basis any flight service station except in accordance with this section.

(b) During the period beginning on the date of enactment of this title and ending on September 30, 1983, the Secretary may provide for the part-time operation of not more than sixty existing flight service stations operated by the Federal Aviation Administration. The operation of a flight service station on a part-time basis shall be subject to the condition that during any period when a flight service station is part-timed, the service provided to airmen with respect to information relating to temperature, dewpoint, barometric pressure, ceiling, visibility, and wind direction and velocity for the area served by such station shall be as good as or better than the service provided when the station is open, and all such service shall be provided either by mechanical device or by contract with another party.

(c) The Secretary may close not more than five existing flight service stations before October 1, 1983. After October 1, 1983, the Secretary may close additional flight service stations, but only if the service provided to airmen after the closure of such station with respect to information relating to temperature, dewpoint, barometric pres-

sure, ceiling, visibility, and wind direction and velocity for the area served by such station is as good as or better than the service provided when the station was open and such service is provided either by mechanical device or by contract with another party.

SEC. 529. EXPLOSIVE DETECTION K-9 TEAMS.

The Secretary shall provide by grant for the continuation of the Explosive Detection K–9 Team Training Program for the purpose of detecting explosives at airports and aboard aircraft. There is authorized to be appropriated out of the Airport and Airway Trust Fund for purposes of this section not more than $150,000 nor less than $130,000 for each fiscal year beginning after September 30, 1981, and ending before October 1, 1987.

SEC. 530. RELEASE OF CERTAIN CONDITIONS.

(a) CRYSTAL CITY, TEXAS.—(1) Notwithstanding section 16 of the Federal Airport Act (as in effect on January 3, 1949), the Secretary of Transportation is authorized, subject to the provisions of section 4 of the Act of October 1, 1949 (50 App. U.S.C. 1622c), and the provisions of paragraph (2) of this subsection, to grant releases from any of the terms, conditions, reservations, and restrictions contained in the deed of conveyance dated January 3, 1949, or any other deed of conveyance dated after such date and before the date of enactment of this section, under which the United States conveyed certain property to Crystal City, Texas, for airport purposes.

(2) Any release granted by the Secretary of Transportation under paragraph (1) of this subsection shall be subject to the following conditions:

(A) Crystal City, Texas, shall agree that in conveying any interest in the property which the United States conveyed to the city by a deed described in paragraph (1) the city will receive an amount for such interest which is equal to the fair market value (as determined pursuant to regulations issued by such Secretary).

(B) Any such amount so received by the city shall be used by the city for the development, improvement, operation, or maintenance of a public airport.

(b) BROWNWOOD, TEXAS.—(1) Notwithstanding section 16 of the Federal Airport Act (as in effect on June 26, 1950), the Secretary of Transportation is authorized, subject to the provisions of section 4 of the Act of October 1, 1949 (50 App. U.S.C. 1622c), and the provisions of paragraph (2) of this subsection, to grant releases from any of the terms, conditions, reservations, and restrictions contained in the deeds of conveyance dated June 26, 1950, and April 1, 1963, under which the United States conveyed certain property to the city of Brownwood, Texas, for airport purposes.

(2) Any release granted by the Secretary of Transportation under paragraph (1) of this subsection shall be subject to the following conditions:

(A) The city of Brownwood, Texas, shall agree that in conveying any interest in the property which the United States conveyed to the city by the deeds dated June 26, 1950, and April 1, 1963, the city will receive an amount for such interest which is equal to the fair market value (as determined pursuant to regulations issued by such Secretary).

(B) Any such amount so received by the city shall be used by the city for the development, improvement, operation, or maintenance of a public airport.

(c) Grand Junction, Colorado.—(1) Notwithstanding section 16 of the Federal Airport Act (as in effect on September 14, 1951), the Secretary of Transportation is authorized, subject to the provisions of section 4 of the Act of October 1, 1949 (50 App. U.S.C. 1622c), and the provisions of paragraph (2) of this subsection, to grant releases from any of the terms, conditions, reservations, and restrictions contained in the deed of conveyance dated September 14, 1951, under which the United States conveyed certain property to the city of Grand Junction, Colorado, for airport purposes and the deed of conveyance dated March 24, 1975, under which the city of Grand Junction, Colorado, conveyed such property to the Walker Field Public Airport Authority.

(2) Any release granted by the Secretary of Transportation under paragraph (1) of this subsection shall be subject to the following conditions:

(A) The property for which releases are granted under this section shall not exceed a total of eighteen acres.

(B) The Walker Field Public Airport Authority shall agree that in leasing, or conveying any interest in, the property for which releases are granted under this section, such Authority will receive an amount which is equal to the fair lease value or the fair market value, as the case may be (as determined pursuant to regulations issued by such Secretary).

(C) Any such amount so received by the Walker Field Public Airport Authority, shall be used by such Authority for the development, improvement, operation, or maintenance of the Walker Field Public Airport.

(d) Newport, Arkansas.—(1) Notwithstanding section 16 of the Federal Airport Act (as in effect on December 17, 1947), the Secretary of Transportation is authorized, subject to the provisions of section 4 of the Act of October 1, 1949 (50 App. U.S.C. 1622c), and the provisions of paragraph (2) of this subsection, to grant releases from any of the terms, conditions, reservations, and restrictions contained in the deed of conveyance dated December 17, 1947, or any other deed of conveyance dated after such date and before the date of enactment of this section, under which the United States conveyed certain property to Newport, Arkansas, for airport purposes.

(2) Any release granted by the Secretary of Transportation under paragraph (1) of this subsection shall be subject to the following conditions:

(A) Newport, Arkansas, shall agree that in conveying any interest in the property which the United States conveyed to the city by a deed described in paragraph (1) the city will receive an amount for such interest which is equal to the fair market value (as determined pursuant to regulations issued by such Secretary).

(B) Any such amount so received by the city shall be used by the city for the development, improvement, operation, or maintenance of a public airport.

SEC. 531. CONTINUATION OF CERTAIN CERTIFICATES.

Notwithstanding any other provision of law or of any certificate issued by the Civil Aeronautics Board to the contrary, any certificate to engage in temporary air transportation which was issued under section 401(d)(8) of the Federal Aviation Act of 1958 or pursuant to the Trans-Atlantic Route Proceeding, CAB Docket Number 25908, and any certificate which was issued in the California/Southwest-Mexico Route Proceeding, CAB Docket Number 32665, and which is in effect on the date of enactment of this title shall be effective for a period of two years beyond the period for which it was issued.

SEC. 532. STATE TAXATION.

(a) Section 1113(b) of the Federal Aviation Act of 1958 (49 U.S.C. 1513(b)) is amended by striking out "Nothing" and inserting in lieu thereof "Except as provided in subsection (d) of this section, nothing".

(b) Section 1113 of such Act is further amended by adding at the end thereof the following new subsection:

"(d)(1) The following acts unreasonably burden and discriminate against interstate commerce and a State, subdivision of a State, or authority acting for a State or subdivision of a State may not do any of them:

"(A) assess air carrier transportation property at a value that has a higher ratio to the true market value of the air carrier transportation property than the ratio that the assessed value of other commercial and industrial property of the same type in the same assessment jurisdiction has to the true market value of the other commercial and industrial property;

"(B) levy or collect a tax on an assessment that may not be made under subparagraph (A) of this paragraph; or

"(C) levy or collect an ad valorem property tax on air carrier transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.

"(2) In this subsection—

"(A) 'assessment' means valuation for a property tax levied by a taxing district;

"(B) 'assessment jurisdiction' means a geographical area in a State used in determining the assessed value of property for ad valorem taxation;

"(C) 'air carrier transportation property' means property, as defined by the Civil Aeronautics Board, owned or used by an air carrier providing air transportation;

"(D) 'commercial and industrial property' means property, other than transportation property and land used primarily for agricultural purposes or timber growing, devoted to a commercial or industrial use and subject to a property tax levy; and

"(E) 'State' shall include the Commonwealth of Puerto Rico, the Virgin Islands, Guam, the District of Columbia, the territories or possessions of the United States, and political agencies of two or more States.

"(3) This subsection shall not apply to any in lieu tax which is wholly utilized for airport and aeronautical purposes.".

TITLE VI—FEDERAL SUPPLEMENTAL COMPENSATION PROGRAM

Subtitle A—Extension of Benefits

SHORT TITLE

SEC. 601. This subtitle may be cited as the "Federal Supplemental Compensation Act of 1982".

FEDERAL-STATE AGREEMENTS

SEC. 602. (a) Any State which desires to do so may enter into and participate in an aggreement with the Secretary of Labor (hereinafter in this title referred to as the "Secretary") under this subtitle. Any State which is a party to an agreement under this subtitle may, upon providing thirty days' written notice to the Secretary, terminate such agreement.

(b) Any such agreement shall provide that the State agency of the State will make payments of Federal supplemental compensation—

(1) to individiuals who—

(A) have exhausted all rights to regular compensation under the State law;

(B) have no rights to compensation (including both regular compensation and extended compensation) with respect to a week under such law or any other State unemployment compensation law or to compensation under any other Federal law (and is not paid or entitled to be paid any additional compensation under any such State or Federal law); and

(C) are not receiving compensation with respect to such week under the unemployment compensation law of Canada;

(2) for any week of unemployment which begins in the individual's period of eligibility,

except that no payment of Federal supplemental compensation shall be made to any individual for any week of unemployment which begins more than two years after the end of the benefit year for which he exhausted his rights to regular compensation.

(c) For purposes of subsection (b)(1)(A), an individual shall be deemed to have exhausted his rights to regular compensation under a State law when—

(A) no payments of regular compensation can be made under such law because such individual has received all regular compensation available to him based on employment or wages during his base period; or

(B) his rights to such compensation have been terminated by reason of the expiration of the benefit year with respect to which such rights existed.

(d) For purposes of any agreement under this subtitle—

(1) the amount of the Federal supplemental compensation which shall be payable to any individual for any week of total unemployment shall be equal to the amount of the regular com-

pensation (including dependents' allowances) payable to him during his benefit year under the State law for a week of total unemployment; and

(2) the terms and conditions of the State law which apply to claims for extended compensation and to the payment thereof shall apply to claims for Federal supplemental compensation and the payment thereof; except where inconsistent with the provisions of this subtitle or with the regulations of the Secretary promulgated to carry out this subtitle.

Solely for purposes of paragraph (2), the amendment made by section 2404(a) of the Omnibus Budget Reconciliation Act of 1981 shall be deemed to be in effect for all weeks beginning on or after September 12, 1982.

(e)(1) Any agreement under this subtitle with a State shall provide that the State will establish, for each eligible individual who files an application for Federal supplemental compensation, a Federal supplemental compensation account with respect to such individual's benefit year.

(2)(A) Except as otherwise provided in this paragraph, the amount established in such account for any individual shall be equal to the lesser of—

(i) 50 per centum of the total amount of regular compensation (including dependents' allowances) payable to him with respect to the benefit year (as determined under the State law) on the basis of which he most recently received regular compensation; or

(ii) 6 times his average weekly benefit amount (as determined for purposes of section 202(b)(1)(C) of the Federal-State Extended Unemployment Compensation Act of 1970) for his benefit year.

(B) If an extended benefit period was in effect under the Federal-State Extended Unemployment Compensation Act of 1970 in a State for any week which begins on or after June 1, 1982, and before the week for which the compensation is paid, subparagraph (A) shall be applied with respect to such State by substituting "10" for "6" in clause (ii) thereof.

(C)(i) In the case of any State not described in subparagraph (B), subparagraph (A) shall be applied, only with respect to weeks during a high unemployment period, by substituting "8" for "6" in clause (ii) thereof.

(ii) For purposes of clause (i), the term "high unemployment period" means, with respect to any State, the period—

(I) which begins with the third week after the first week in which the rate of insured unemployment in the State for the period consisting of such week and the immediately preceding 12 weeks equals or exceeds 3.5 percent, and

(II) which ends with the third week after the first week in which the rate of insured unemployment in the State for the period consisting of such week and the immediately preceding 12 weeks is less than 3.5 percent;

except that no high unemployment period shall last for a period of less than 4 weeks.

(iii) For purposes of clause (ii), the rate of insured unemployment for any period shall be determined in the same manner as deter-

mined for purposes of section 203 of the Federal-State Extended Unemployment Compensation Act of 1970.

(f)(1) No Federal supplemental compensation shall be payable to any individual under an agreement entered into under this subtitle for any week beginning before whichever of the following is the later:

(A) the week following the week in which such agreement is entered into; or

(B) September 12, 1982.

(2) No Federal supplemental compensation shall be payable to any individual under an agreement entered into under this subtitle for any week beginning after March 31, 1983.

PAYMENTS TO STATES HAVING AGREEMENTS FOR THE PAYMENT OF FEDERAL SUPPLEMENTAL COMPENSATION

Sec. 603. (a) There shall be paid to each State which has entered into an agreement under this subtitle an amount equal to 100 per centum of the Federal supplemental compensation paid to individuals by the State pursuant to such agreement.

(b) No payment shall be made to any State under this section in respect of compensation to the extent the State is entitled to reimbursement in respect of such compensation under the provisions of any Federal law other than this subtitle or chapter 85 of title 5 of the United States Code. A State shall not be entitled to any reimbursement under such chapter 85 in respect of any compensation to the extent the State is entitled to reimbursement under this subtitle in respect of such compensation.

(c) Sums payable to any State by reason of such State's having an agreement under this subtitle shall be payable, either in advance or by way of reimbursement (as may be determined by the Secretary), in such amounts as the Secretary estimates the State will be entitled to receive under this subtitle for each calendar month, reduced or increased, as the case may be, by any amount by which the Secretary finds that his estimates for any prior calendar month were greater or less than the amounts which should have been paid to the State. Such estimates may be made on the basis of such statistical sampling, or other method as may be agreed upon by the Secretary and the State agency of the State involved.

FINANCING PROVISIONS

Sec. 604. (a)(1) Funds in the extended unemployment compensation account (as established by section 905 of the Social Security Act) of the Unemployment Trust Fund shall be used for the making of payments to States having agreements entered into under this Act.

(2) The Secretary shall from time to time certify to the Secretary of the Treasury for payment to each State the sums payable to such State under this Act. The Secretary of the Treasury, prior to audit or settlement by the General Accounting Office, shall make payments to the State in accordance with such certification, by transfers from the extended unemployment compensation account (as established by section 905 of the Social Security Act) to the account of such State in the Unemployment Trust Fund.

(b) There are hereby authorized to be appropriated, without fiscal year limitation, to the extended unemployment compensation account, such sums as may be necessary to carry out the purposes of this Act. Amounts appropriated pursuant to the preceding sentence shall not be required to be repaid.

(c) There are hereby authorized to be appropriated from the general fund of the Treasury, without fiscal year limitation, such funds as may be necessary for purposes of assisting States (as provided in title III of the Social Security Act) in meeting the costs of administration of agreements under this subtitle.

DEFINITIONS

Sec. 605. For purposes of this title—

(1) the terms "compensation", "regular compensation", "extended compensation", "base period", "benefit year", "State", "State agency", "State law", and "week" shall have the meanings assigned to them under section 205 of the Federal-State Extended Unemployment Compensation Act of 1970; and

(2) the term "period of eligibility" means, with respect to any individual, any week which begins on or after September 12, 1982, and begins before April 1, 1983; except that an individual shall not have a period of eligibility unless—

(A) his benefit year ends on or after June 1, 1982, or

(B) such individual was entitled to extended compensation for a week which begins on or after June 1, 1982.

FRAUD AND OVERPAYMENTS

Sec. 606. (a)(1) If an individual knowingly has made, or caused to be made by another, a false statement or representation of a material fact, or knowingly has failed, or caused another to fail, to disclose a material fact, and as a result of such false statement or representation or of such nondisclosure such individual has received an amount of Federal supplemental compensation under this subtitle to which he was not entitled, such individual—

(A) shall be ineligible for further Federal supplemental compensation under this subtitle in accordance with the provisions of the applicable State unemployment compensation law relating to fraud in connection with a claim for unemployment compensation; and

(B) shall be subject to prosecution under section 1001 of title 18, United States Code.

(2)(A) In the case of individuals who have received amounts of Federal supplemental compensation under this subtitle to which they were not entitled, the State is authorized to require such individuals to repay the amounts of such Federal supplemental compensation to the State agency, except that the State agency may waive such repayment if it determines that—

(i) the payment of such Federal Supplemental compensation was without fault on the part of any such individual, and

(ii) such repayment would be contrary to equity and good conscience.

(B) The State agency may recover the amount to be repaid, or any part thereof, by deductions from any Federal supplemental compen-

sation payable to such individual under this subtitle or from any unemployment compensation payable to such individual under any Federal unemployment compensation law administered by the State agency or under any other Federal law administered by the State agency which provides for the payment of any assistance or allowance with respect to any week of unemployment, during the three-year period after the date such individuals received the payment of the Federal supplemental compensation to which they were not entitled, except that no single deduction may exceed 50 per centum of the weekly benefit amount from which such deduction is made.

(C) No repayment shall be required, and no deduction shall be made, until a determination has been made, notice thereof and an opportunity for a fair hearing has been given to the individual, and the determination has become final.

(3) Any determination by a State agency under paragraph (1) or (2) shall be subject to review in the same manner and to the same extent as determinations under the State unemployment compensation law, and only in that manner and to that extent.

Subtitle B—Taxation of Unemployment Compensation

SEC. 611. TAXATION OF UNEMPLOYMENT COMPENSATION.

(a) LOWERING BASE AMOUNT FROM $20,000 TO $12,000 (FROM $25,000 TO $18,000 IN CASE OF JOINT RETURN).—Subsection (b) of section 85 (defining base amount) is amended—

(1) by striking out "$20,000" and inserting in lieu thereof "$12,000", and

(2) by striking out "$25,000" and inserting in lieu thereof "$18,000".

(b) EFFECTIVE DATES.—

(1) COMPENSATION PAID AFTER 1981.—The amendments made by this section shall apply to payments of unemployment compensation made after December 31, 1981, in taxable years ending after such date.

(2) NO ADDITION TO TAX FOR UNDERPAYMENT OF ESTIMATED TAX ATTRIBUTABLE TO APPLICATION OF AMENDMENTS TO COMPENSATION PAID IN 1982.—No addition to tax shall be made under section 6654 of the Internal Revenue Code of 1954 with respect to any underpayment to the extent such underpayment is attributable to unemployment compensation which is received during 1982 and which (but for the amendments made by subsection (a)) would not be includable in gross income.

(3) SPECIAL RULE FOR FISCAL YEAR TAXPAYERS.—In the case of a taxable year (other than a calendar year) which includes January 1, 1982—

(A) the amendments made by this section shall be applied by taking into account the entire amount of unemployment compensation received during such taxable year, but

(B) the increase in gross income for such taxable year as a result of such amendments shall not exceed the amount of unemployment compensation paid after December 31, 1981.

(4) UNEMPLOYMENT COMPENSATION DEFINED.—For purposes of this subsection, the term "unemployment compensation" has the

meaning given to such term by section 85(c) of the Internal Revenue Code of 1954.

And the Senate agree to the same.

That the House recede from its disagreement to the amendment of the Senate to the title of the bill.

Committee on Ways and Means for the entire bill and the Senate amendment and modifications committed to conference, with the exception of subtitle B (Medicaid) of title I and title IV (Airport and Airway System Development) except for section 406(e) of that title and with the exception of section 395 of the Senate amendment and modifications committed to conference.

Dan Rostenkowski,
Sam Gibbons,
J. J. Pickle,
Charles B. Rangel,
Pete Stark,
Barber B. Conable, Jr.,

Committee on Energy and Commerce solely for the consideration of subtitle B of title I (Medicaid), of the Senate amendment and modifications committed to conference and subtitle C of title I (Utilization and Quality Control Peer Review) of the Senate amendment and the modifications committed to conference and such parts of subtitle A (Medicare) of title I of the Senate amendment and modifications committed to conference that relate to amendments to the supplementary medical insurance program authorized under title XVIII of the Social Security Act:

John D. Dingell,
Henry A. Waxman,
James H. Scheuer,
Jim Broyhill,
Ed Madigan,

Committee on Energy and Commerce solely for consideration of section 395 of the Senate amendment and modifications committed to conference:

John D. Dingell,
Timothy E. Wirth,
James T. Broyhill,

Committee on Public Works and Transportation solely for the consideration of title IV of the Senate amendment and modifications committed to conference with the exception of sections 406(e) and 407(b) of that title:

Norman Y. Mineta,
Glenn M. Anderson,
Elliott H. Levitas,
James L. Oberstar,
Don Clausen,
Gene Snyder,
John Paul Hammerschmidt,

Soley for the consideration of section 407(b) title IV of the Senate amendment and modifications committed to conference:

Don Fuqua,
Dan Glickman,
Larry Winn, Jr.,
Managers on the Part of the House.

For the entire bill with the exception of title IV (Airport and airway system development) except for section 406(e):

Bob Dole,
Bob Packwood,
Bill Roth,
John C. Danforth,
Russell B. Long,
Lloyd Bentsen,

Solely for consideration of title IV (excluding section 406(e)):

Bob Packwood,
Nancy Landon Kassebaum,
Howard W. Cannon,
Managers on the Part of the Senate.

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JOINT EXPLANATORY STATEMENT OF THE COMMITTEE OF CONFERENCE

The managers on the part of the House and the Senate at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 4961) to make miscellaneous changes in the tax laws, and for other purposes, submit the following joint statement to the House and the Senate in explanation of the effect of the action agreed upon by the managers and recommended in the accompanying conference report:

The Senate amendment to the text of the bill struck out all of the House bill after the enacting clause and inserted a substitute text.

The House recedes from its disagreement to the amendment of the Senate with an amendment which is a substitute for the House bill and the Senate amendment. The differences between the House bill, the Senate amendment, and the substitute agreed to in conference are noted below, except for clerical corrections, conforming changes made necessary by agreements reached by the conferees, and minor drafting and clarifying changes.

CONTENTS FOR STATEMENT OF MANAGERS

Page

PART ONE: Spending Reduction Provisions Relating to Savings in Health and Income Security Programs (Title I); Unemployment Compensation Extension Provisions (Title VI) 411

PART TWO: Revenue Provisions (Titles II, III, and IV) . 467

PART THREE: Airport and Airway Improvement Provisions (Title V) 697

PART ONE

CONTENTS OF SPENDING REDUCTION PROVISIONS

TITLE I

A. MEDICARE

Page

1. One-month delay in entitlement to medicare benefits ... 414
2. Medicare payments secondary for older workers choosing to remain covered under group health plans ... 414
3. Five-percent copayments for home health services... 415
4. Reimbursement for inpatient radiology and pathology services ... 415
5. Increase in part B deductible ... 415
6. Limitation on physician fee economic index ... 416
7. Elimination of inpatient routine nursing salary cost differential ... 416
8. Reimbursement of provider-based physicians ... 416
9. Part B premium as a constant percentage of costs ... 417
10. Medicare reimbursement to hospitals ... 417
11. Elimination of private room subsidy ... 422
12.–13. Single reimbursement limits for skilled nursing facilities and home health agencies ... 423
14. Elimination of duplicate payments for outpatient services ... 423
15. Audit and medical claims review ... 424
16. Temporary delay in periodic interim payments ... 424
17. Reimbursement of assistants at surgery ... 424
18. Judicial review of decision by provider reimbursement review board ... 425
19. Prohibition of payment for ineffective drugs ... 425
20. Medicare payments to health maintenance organizations (HMOs) ... 425
21. Technical corrections relating to medicare ... 425
22. Hospice care ... 428
23. Coverage of extended care services without regard to 3-day prior hospitalization requirement ... 430
24. Prohibiting recognition of payments under certain percentage arrangements ... 430
25. Interest charges on overpayments and underpayments ... 431

CONTENTS OF SPENDING REDUCTION PROVISIONS—Continued

A. MEDICARE—Continued

Page
26. Prohibiting payment for Hill-Burton free care.......... 431
27. Prohibiting payment for anti-unionization activities.......... 431
28. Eliminating "lesser of cost or charge" provision....... 432
29. Extending medicare proficiency examination authority.......... 432
30. Prohibiting retroactivity of regulations regarding access to books and records.......... 433
31. Health Care Financing Administration/private sector utilization review initiative.......... 433
32. Special part B enrollment without penalty.......... 434

B. MEDICAID

1. Copayments by medicaid recipients.......... 434
2. Elimination of Federal matching for medicare part B buy-in.......... 436
3. Modify lien provision.......... 436
4. Limitation on Federal financial participation in erroneous medical assistance expenditures.......... 439
5. Optional medicaid coverage for individuals who would have qualified for AFDC but for amendments to the earned income disregard and related provisions.......... 439
6. Medicaid coverage of home care of certain disabled children.......... 440
7. Technical corrections relating to medicaid.......... 440
8. Medicaid funding in American Samoa.......... 441
9. Nursing home deregulation moratorium.......... 441

C. UTILIZATION AND QUALITY CONTROL PEER REVIEW

1. Establishment of utilization and quality control peer review program.......... 442

D. AID TO FAMILIES WITH DEPENDENT CHILDREN

1. Rounding of eligibility and benefit amounts.......... 444
2. Effective date of application; proration of first month's benefit.......... 444
3. Absence from home solely by reason of uniformed service.......... 444
4. Sanction for termination or reduction of employment.......... 444
5. Job search.......... 445
6. Inclusion and exclusion of specified individuals' needs and income.......... 446
7. Repeal of emergency assistance program.......... 447
8. Proration of standard amount for shelter and utilities.......... 448
9. Limitation on Federal financial participation in erroneous assistance expenditures.......... 448
10. Households headed by minor parents.......... 449
11. Exclusion from income of certain State payments.... 449

CONTENTS OF SPENDING REDUCTION PROVISIONS—Continued

D. Aid to Families With Dependent Children—Continued

Page
12. Extension of time for States to establish a work incentive demonstration program 450
13. Exclusion from income 450
14. Technical amendments to social services and foster care provisions in 1981 Reconciliation Act 451

E. Child Support Enforcement

1. Fee for services to non-AFDC families 452
2. Allotments from pay for child and spousal support owed by members of the uniformed services on active duty 452
3. Reimbursement of State agency in initial month of ineligibility for AFDC 453
4. Reduction in certain Federal payments to States under the child support enforcement program 453
5. Technical amendments to child support enforcement provisions in 1981 Reconciliation Act 454

F. Supplemental Security Income

1. Proration of initial SSI benefit payment 454
2. Rounding of SSI eligibility and benefit amounts 454
3. Coordination of SSI and OASDI cost-of-living adjustments 454
4. Phaseout of hold harmless protection 454
5. Recovery of SSI overpayments 456
6. Exclusion from resources of burial plots and certain funds set aside for burial expenses 456
7. Mandatory passthrough under State supplementation provisions 457
8. Treatment of unnegotiated checks under the supplemental security income program 457

G. Unemployment Compensation

1. Rounding of unemployment benefits to next lowest dollar 458
2. Use of amounts transferred to State unemployment funds pursuant to the Reed Act 458
3. Unemployment benefits paid to ex-service members 459
4. Additional weeks of unemployment compensation benefits: Federal supplemental benefits 459
5. Taxation of unemployment compensation 461
6. Interest on State unemployment loans transferred to Extended Unemployment Compensation Account (EUCA) 462
7. Treatment of certain employees of institutions of higher education 462
8. Short-time compensation 463

TITLE I—PROVISIONS RELATING TO SAVINGS IN HEALTH AND INCOME SECURITY PROGRAMS

SUBTITLE A—MEDICARE

1. One month delay in entitlement to medicare benefits

Senate amendment

The Senate amendment defers eligibility for parts A and B of medicare until the first day of the month following the month in which an individual attains age 65.

The provision would be effective with respect to individuals reaching age 65 after August 1982.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

2. Medicare payments secondary for older workers choosing to remain covered under group health plans

Senate amendment

The Senate provision amends the Federal Age Discrimination in Employment Act (ADEA) to require employers to offer their employees age 65 through 69 and their dependents the same health benefits as are offered to their younger employees. The provision makes medicare the secondary payor for such employees (and their spouses) age 65 through 69. The provision would not apply to employers with less than 20 employees.

Medicare's payment for any item or service furnished to an employee (or his or her spouse) would be reduced where the combined payment under medicare and the employer's health benefits plan would otherwise exceed an amount equal to: (1) for items or services reimbursed on a cost or cost-related basis, their reasonable cost; or, (2) for items reimbursed on a charge basis, the higher of the reasonable charge (or other amount payable under medicare, without regard to the program deductibles or coinsurance) or the amount payable under the employer group plan (without regard to deductibles or coinsurance imposed under that plan). In no case would medicare pay more than medicare would have paid in the absence of any employer plan coverage. This provision would be effective January 1, 1983.

House bill

No provision.

Conference agreement

The conference agreement includes the Senate amendment. It is the intent of the conferees that an employee will have the option of rejecting the plan offered by the employer, thereby, retaining medicare as primary coverage. It is the understanding of the conferees that the Secretary of Labor will promulgate regulations to prevent employers from offering a group health insurance plan or option which is designed to circumvent this provision in an attempt to induce employees to reject the employer general health benefit plan offered to other employees under the age of 65.

3. Five-percent copayments for home health services

Senate amendment

The Senate amendment imposes copayments on home health services equal to 5 percent of the average reasonable cost per visit, beginning with the twentieth visit made with respect to an individual in a calendar year. The provision would be effective with respect to services furnished on or after January 1, 1983.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

4. Reimbursement for inpatient radiology and pathology services

Senate amendment

The Senate amendment eliminates the 100 percent reimbursement rate currently applicable to services provided to hospital inpatients that are furnished by radiologists and pathologists who accept assignment in all cases for these services. Thus, medicare will pay for such services on the same basis as for other physicians' services, i.e. 80 percent of the reasonable charge after the part B deductible has been met. The provision is effective with respect to services furnished on or after October 1, 1982.

House committee provision

Same provision.

Conference agreement

The conference agreement includes the Senate amendment.

5. Increase in part B deductible

Senate amendment

The Senate amendment increases the Part B deductible for calendar year 1984 to $78 and for 1985 and subsequent calendar years to $80.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

6. Limitation on physician fee economic index

Senate amendment

The Senate amendment provides that (1) the increase in the physician economic index effective July 1, 1982 would not be in effect for charges for services rendered on or after October 1, 1982; (2) the increase allowed for the 12-month period beginning July 1, 1983 could not exceed five percent; and (3) the Secretary of the Department of Health and Human Services would be required to report to the Congress changes in the rate of assignment and in costs paid by beneficiaries as a result of changes made in physician reimbursement.

House committee provision

Under the House committee provision (1) the increase in the economic index for prevailing fees effective July 1, 1982 would be reduced to 4 percent effective October 1, 1982; (2) physicians who agree to accept assignment on all their bills would not be subject to this reduction; and (3) the date of the annual update in the customary and prevailing charge screens would be delayed from July 1, until October 1 of each year, starting in 1983.

Conference agreement

The conference agreement does not include either provision.

7. Elimination of inpatient routine nursing salary cost differential

Senate amendment

The Senate amendment eliminates the routine nursing salary cost differential paid to hospitals and skilled nursing facilities. The provision would be effective October 1, 1982.

House bill

No provision.

Conference agreement

The conference agreement includes the Senate amendment.

8. Reimbursement of provider-based physicians

Senate amendment

The Senate amendment directs the Secretary to prescribe regulations, effective no later than October 1, 1982, which will distinguish between (1) professional medical services which require performance of the physician in person; which are personally rendered to individual patients; which contribute to the patients' diagnosis and treatment; and are reimbursable only under part B on a charge basis, and (2) the professional medical services of practitioners which are of benefit to patients generally and other services not discussed in (1) above which can be reimbursed only on a reasonable cost basis. The amendment provides that reasonable cost reimbursement for provider-based services cannot exceed a reasonable compensation equivalent which shall be established by the Secretary in regulations and shall be based on reasonable annual compensation levels for a full-time equivalent practice in the specialty involved, or on such other basis as the Secretary may approve.

House bill

No provision.

Conference agreement

The conference agreement includes the Senate amendment with minor modifications. The agreement directs the Secretary to prescribe regulations which will distinguish between (1) professional medical services which are personally rendered to an individual patient, which contribute to the patient's diagnosis or treatment, and are reimbursable only under part B on a charge basis; and (2) professional services which are of benefit to patients generally and which can be reimbursed only on a reasonable cost basis. Reasonable cost reimbursement for provider-based services could not exceed a reasonable compensation equivalent established by the Secretary in regulations. The conference agreement directs that regulations implementing this provision be published and effective by October 1, 1982. The conferees understand that such regulations are already under preparation by HHS. The publication and timely implementation of these regulations would reflect the intent of the conferees.

9. Part B premium as a constant percentage of costs

Senate amendment

The Senate amendment would suspend the current limitation on annual increases in the part B premium and instead increase the premium on October 1, 1982, on July 1, 1983, and on July 1, 1984 to a level which will result in monthly premiums which are in the aggregate equal to 25 percent of program costs for aged beneficiaries. During this period, premium increases would not be limited to the lower of the percentage by which cash social security benefits most recently increased, or the increase in the costs of the program as is required by present law. The present law limitation and method of calculating premiums would resume on July 1, 1985.

House bill

No provision.

Conference agreement

The conference agreement includes the Senate amendment with a modification allowing no premium increase before July 1, 1983.

10. Medicare reimbursement to hospitals

(A) EXPANSION OF SECTION 223 LIMITS TO INCLUDE ANCILLARY COSTS

Senate amendment

The Senate amendment extends the so-called Section 223 limitation of present law to ancillary service operating costs, effective with hospital cost reporting periods beginning on or after October 1, 1982. The new limitation would be applied on an average cost-per-case basis and each hospital's limit would be modified by a case-mix adjustment. In no case would payment on a cost-per-case basis be reduced below the allowable cost-per-case reimbursement for the hospital's cost reporting period that immediately precedes the first cost reporting period to which the new limitation is applicable. The limitation would be set at 110 percent of the mean for hospitals of the same type. The Secretary would be required to provide appropriate exemptions, exceptions and adjustments including an adjustment for the special needs of hospitals that incur additional costs in treating low-income patients. Rural hospitals with less than 50 beds would be exempted from the limitations.

House committee provision

The House committee provision is similar to the Senate amendment except that the limitation would be set at 120 percent of the mean in fiscal year 1983, and the Secretary would be authorized to reduce the limitation to 115 percent in fiscal year 1984 and to 110 percent in fiscal year 1985. Provisions similar to those in the Senate amendment are included regarding exemptions, exceptions and adjustments, except that the House provision specifically requires appropriate adjustments for the special needs of psychiatric hospitals and hospitals serving a significantly disproportionate number of low-income or medicare patients. Hospitals in operation with less than 50 beds, on the date of enactment, would be exempted from the limitation without regard to location.

Conference agreement

The conference agreement follows the Senate amendment, under which the current Section 223 limitation would be extended to include ancillary service operating costs, applied on an average cost-per-case basis, and adjusted for case-mix, effective with cost reporting periods beginning on or after October 1, 1982. In no case would reimbursement on a cost-per-case basis be reduced below the allowable cost-per-case reimbursement for the hospital's cost reporting period that immediately precedes the first cost reporting period to which the new limitation is applicable. Under the conference agreement, for the first reporting period it becomes effective, the new limitation would be set at 120 percent of the mean for hospitals of the same type; for the second year, the limitation would be 115 percent of the mean; and for the third and subsequent years, the limitation would be 110 percent of the mean.

Appropriate adjustments would be required for the special needs of psychiatric hospitals and hospitals serving a significantly disproportionate number of low-income or medicare patients. Non-SMSA hospitals with less than 50 beds would be excluded. Other appropriate exemptions, exceptions, and adjustments would be required as in the Senate provision including an adjustment to assure that the proposed limits would not be significantly compromised if a hospital reduces its costs by cutting back on the kinds of services it provides directly to its patients (e.g., leasing its clinical laboratory).

The Secretary is expected to recalculate case-mix adjustments periodically. It is understood that initially the Secretary will need to rely on a currently available indicator of case-mix complexity such as the system developed at Yale University. It is expected that the Secretary will continue to evaluate possible methods for adjusting for case-mix and will adopt an improved method when it becomes available.

It is recognized that case-mix adjusted hospital cost data will not be available on a fully current basis, and must be updated to the hospital cost reporting period for which it will be used in establishing limits. It is expected that the Secretary will use estimated actual industry-wide cost increase data to update available data on hospital costs to the cost reporting period to which the limit will be applied; a further adjustment for anticipated cost increases during the year subject to limits will be based on a hospital wage and price index plus one percentage point.

(B) THREE-YEAR HOSPITAL RATE OF INCREASE PROVISION

Senate amendment

The Senate amendment places an overall limit on annual increases in a hospital's medicare reimbursement on a per case basis, effective for three hospital reporting periods beginning with hospital cost reporting periods beginning on or after October 1, 1982. For the first 2 cost reporting periods, hospitals would be paid 25 percent of their costs in excess of their limits, but none of the excess would be reimbursed in the third year.

The maximum allowable increase is the previous year's allowable costs (or, after the first year, the previous year's limitation ceiling amount) increased by the percentage increase in the hospital wage and price index plus 2 percentage points.

The Secretary is required to provide for exemptions, exceptions, and adjustments from the limits in cases where events beyond the hospital's control or extraordinary circumstances, including changes in the case mix of such hospital, distort the hospital's increase in costs.

House committee provision

The House committee provision establishes a target reimbursement system under which hospitals with operating costs (per case) below the target rate would be paid their costs plus a bonus of 50 percent of the savings (but not to exceed 5 percent of the target rate), and hospitals with costs above the target rate would be paid 50 percent of excess costs (up to 105 percent of target), 25 percent of excess costs (between 105 and 110 percent of target) and none of costs above 110 percent of target. These payments are subject to Section 223 limitations.

The target rate is the previous year's allowable costs (or, after the first year, the previous year's target amount) increased by the percentage increase in the hospital wage and price index plus 1 percentage point.

The Secretary is authorized to provide appropriate exceptions and adjustments to the target rate, specifically including an adjustment for psychiatric hospitals.

The target system applies to reimbursement in the Federal fiscal years 1983, 1984, and 1985, regardless of the period covered by the individual hospital's fiscal year, but ceases upon implementation of a prospective payment system.

Conference agreement

Under the conference agreement, a target rate reimbursement system would be established applicable to a hospital's first three cost reporting periods beginning on or after October 1, 1982. Under the provision, the target rate would be the previous year's allowable operating costs per case (or, after the first year, the previous year's target amount) increased by the percentage increase in the hospital wage and price index plus one percentage point. A hospital with operating costs below the target rate would be paid its costs plus a bonus of 50 percent of the savings (but not to exceed 5 percent of the target rate); a hospital with costs above the target rate would be allowed 25 percent of its cost in excess of the target for the first 2 years; none of the excess would be reimbursed in the third year. Provider payments under the target reimbursement system could not exceed the amount payable under the new section 223 limitations.

The Secretary of HHS would be required to provide for appropriate exemptions, exceptions, and adjustments as in the Senate provision. The conferees note that adjustments could have the effect of either increasing or decreasing the target payment amount. The principal intention in authorizing such adjustments is to take into account factors that would distort either a hospital's base period or rate of cost increase in any of the three years to which the provisions are applicable. Examples of such factors include significant changes in a hospital's case-mix in a particular year when compared to the base year, extraordinary circumstances beyond the hospital's control, and a reduction in a hospital's costs resulting from cutting back on the kinds of services directly provided to patients—e.g., as the result of leasing out its clinical laboratory.

Because the proposed target rates of increase and the new section 223 limits would be determined on a per case basis, an incentive would be created to increase admissions or discharges. It is anticipated that the Secretary will give consideration to making an adjustment where a hospital manipulates admissions or discharges in order to maximize reimbursement.

Because both the new limitation on total inpatient operating costs (the expanded section 223 limitations) and the target reimbursement provisions begin as early as October 1, 1982 for hospitals with cost reporting periods beginning on that date, it is recognized that the Secretary will have limited time to prepare for implementation of these new reimbursement provisions. Accordingly, the conference agreement authorizes the Secretary to proceed to implementation on the basis of final regulations issued without the customary prior comment period. However, it is expected that comments on the final regulations will be solicited and that appropriate revisions will be made based on the comments received.

Similarly, time may not permit the normal process of approval of forms to take place under the provisions of the Paperwork Reduction Act of 1980 (P.L. 96-511). Accordingly, all revisions to the medicare cost reporting forms necessary to implement these new reimbursement provisions would be exempt from the Act until the end of calendar year 1983, after which it is expected that the Paperwork Reduction Act will be complied with in the normal manner.

In the case of hospitals currently under the OASDHI program which withdraw after August 15, 1982, the Secretary of HHS is required to compute a reduction in the amount of payments otherwise made to reflect the savings in costs achieved through withdrawals. This reduction can be offset by demonstrated expenditures for pension, health, and insurance benefits which are comparable to, and substituted for, the Social Security benefits.

(C) PROSPECTIVE PAYMENTS FOR HOSPITALS AND SKILLED NURSING FACILITIES

Senate amendment

The Senate amendment requires the Secretary to develop, in consultation with Senate Finance Committee and House Ways and Means Committee, medicare prospective reimbursement proposals for hospitals, skilled nursing facilities and to the extent feasible other providers, and to report to the committees on the proposals within 5 months.

House committee provision

The House committee provision requires the Secretary to develop and to submit to Congress by December 31, 1982, a medicare prospective payment plan for hospital inpatient services and extended care services designed to take effect October 1, 1983, and which, if implemented would not result in any increase in program costs. If submitted on a timely basis, the plan would take effect and replace reimbursement policy under existing law unless disapproved by concurrent resolution of Congress adopted by July 1, 1983.

Conference agreement

The conferees agreed to the Senate provision. Because of the desire of the conferees to proceed as soon as possible with a prospective payment system, it is expected that the administration recommendations, when presented to the Finance Committee and Committee on Ways and Means, will be sufficiently detailed as to be able to serve as a basis for legislation.

(D) RECOGNITION OF STATE HOSPITAL COST CONTROL SYSTEMS

Senate amendment

No provision.

House committee provision

Under the House committee provision, the Secretary would be authorized, at his discretion, to permit payment under an alternative reimbursement system if, upon application by the State, the Secretary determined that (1) the system would apply to substantially all non-Federal acute care hospitals in the State and would apply to the review of at least 75 percent of all revenues or expenses for inpatient hospital services including medicare and medicaid; (2) the Secretary has been provided satisfactory assurances regarding the equitable treatment of all entities that pay hospitals for inpatient services (including medicare and medicaid), together with assurances regarding the equitable treatment of hospital employees and patients; and (3) the Secretary has been provided satisfactory assurances that under the system, over a 36-month period, the amount of payments made under the proposed alternative reimbursement system would not be greater than the amount of payments which would otherwise have been made under medicare. In determining whether an alternative system would result in reimbursement which is less than otherwise would have been paid in a State, the Secretary would be permitted to take into account previous reductions in medicare reimbursement due to the operation of a hospital reimbusement control system if such system has resulted in an aggregate rate of increase in operating costs of inpatient services under medicare which was less than the national aggregate rate of increase in such costs.

Conference agreement

The conference agreement included the House committee provision with a modification with respect to the termination of current medicare waivers. The conferees included the House committee provision to allow the Secretary to take advantage of effective alternative reimbursement systems which have already been implemented or those which may be implemented in the future. Although the provision provides discretion to the Secretary in approving alternative state systems, the conferees expect the Secretary to approve such systems if they meet the criteria set forth in the provision and other criteria as established by the Secretary.

The provision also permits the Secretary to take into account previous reductions in medicare rates of increase due to the operation of a state hospital reimbursement control system. The conferees included this provision because of their concern that State programs which control substantially all revenues other than medicare may have already achieved savings for the medicare program through reducing their overall rate of growth in hospital expenditures.

With respect to the authority provided to the Secretary under current law to establish and continue medicare demonstration projects, the Secretary would be prohibited from terminating a project until six months after he notifies the State of his decision to terminate.

11. Elimination of private room subsidy

Senate amendment

The Senate amendment requires the Secretary to publish regulations which would eliminate the subsidy of private hospital rooms. Medicare currently determines its payments to hospitals on the basis of the average costs of all of a hospital's rooms, including its private accommodations, even though medicare generally is intended to cover only the costs of semi-private room accommodations.

House bill

No provision.

Conference agreement

The conference agreement includes the Senate amendment. The provision is intended to direct the Secretary to implement the provisions of current law. The conferees note that elimination of this subsidy does not alter medicare's policy of covering private rooms when medically necessary, and does not alter the options currently available to States to cover such private rooms under medicaid.

12–13. Single reimbursement limits for skilled nursing facilities and home health agencies

Senate amendment

The Senate amendment requires the Secretary to modify existing regulations which would establish single payment limits for skilled nursing facilities and home health agencies on the basis of the cost experience of free-standing facilities. Separate limits are currently established for such facilities depending on whether they are hospital-based or free-standing facilities.

The amendment would be effective with respect to home health agency cost reporting periods beginning on or after the date of enactment and for skilled nursing facility cost reporting periods beginning on or after October 1, 1982.

House bill

No provision.

Conference agreement

The conference agreement includes the Senate amendment. The conferees intend that in establishing the payment limits the Secretary shall make adjustments, as appropriate, based on legitimate cost differences in hospital-based facilities resulting from such factors as a more complex case-mix or the effects of medicare cost allocation requirements.

14. Elimination of duplicate payments for outpatient services

Senate amendment

The Senate amendment requires the Secretary to issue regulations that would eliminate the duplicate payment of overhead expenses from the recognized charges of a physician who performs services in a hospital's outpatient department. The amendment would be effective with respect to charges for services rendered on or after the date of enactment.

House bill

No provision.

Conference agreement

The conference agreement includes the Senate amendment.

15. Audit and medical claims review

Senate amendment

The Senate amendment requires that the medicare contractor budgets for fiscal years 1983, 1984, and 1985 be supplemented by $45 million in each year to be spent specifically for provider cost audits and medical review activities.

House committee provision

Similar provision.

Conference agreement

The conference agreement includes the House committee provision.

16. Temporary delay in periodic interim payments

Senate amendment

The Senate amendment modifies the existing periodic interim payment (PIP) procedure for hospitals by providing for a 3 week delay in the flow of PIP payments during September 1983; a similar deferral is authorized during September 1984.

House committee provision

Similar provision.

Conference agreement

The conference agreement includes the Senate amendment.

17. Reimbursement of assistants at surgery

Senate amendment

The Senate amendment prohibits reasonable charge reimbursement for an assistant at surgery in hospitals where an approved training program exists in the specialty, except under the following exceptional circumstances: (1) the service is complex and requires performance by a team of physicians; (2) the patient has multiple conditions which require the presence of, and active care by, a physician of another specialty during an operation, or (3) in the case of exceptional medical circumstances where qualified house staff are not available to assist at surgery. The Senate provision would be effective with respect to services performed on or after October 1, 1982.

House committee provision

Same provision.

Conference agreement

The conference agreement follows the Senate amendment with a modification under which payment may be made on a reasonable charge basis if the services, as determined by the Secretary: (1) are required due to exceptional medical circumstances; (2) are performed by team physicians needed to perform complex medical procedures; (3) constitute concurrent medical care which requires the presence of, and active care by, a physician of another specialty during surgery; or (4) are required in other circumstances as determined by the Secretary.

18. Judicial review of decision by provider reimbursement review board

Senate amendment

The Senate amendment modifies existing requirements pertaining to judicial review of decisions made by the Provider Reimbursement Review Board (PRRB). Under existing law, judicial actions brought jointly by several providers of services in connection with adverse decisions of the PRRB may be taken only in the U.S. District Court for the District of Columbia. The Senate provision permits Federal judicial review of adverse decisions of the PRRB involving actions brought jointly by several providers of medicare services to be conducted by the U.S. District Court for the district where the "principal party" for the group is located. The provision would be effective on enactment.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

19. Prohibition of payment for ineffective drugs

Senate amendment

The Senate amendment provides for implementation of Section 2103 of the Omnibus Budget Reconciliation Act of 1981 (P.L. 97–35) effective October 1, 1982. Section 2103 prohibited the use of Federal funds under medicare part B and under medicaid to pay for certain less than effective drugs. Subsequent legislation has led to delays in the implementation of this provision.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment, with a modification to make the provision effective September 30, 1982.

20. Medicare payments to health maintenance organizations (HMO's)

Senate amendment

The Senate amendment modifies current law requirements for contracting with health maintenance organizations (HMO's) by authorizing prospective reimbursement under risk sharing contracts with competitive medical plans at a rate equal to 95 percent of the average cost of providing services to a medicare beneficiary in the fee-for-service sector (the adjusted average per capita cost—AAPCC).

The Senate amendment includes the current law definition of eligible beneficiaries except that persons medically determined to have end-stage renal disease are excluded. It defines a competitive medical plan as either a Federally-qualified HMO, a State-licensed HMO, or an organization which meets certain service requirements, receives fixed and periodic payments on behalf of enrollees, provides physician services through staff MDs or MDs under contract, assumes financial risk on a prospective basis and meets financial viability standards.

The Senate amendment changes existing enrollment/disenrollment policies by: (a) requiring an annual open enrollment period of at least 30 days; (b) requiring acceptance of beneficiaries in order of application up to capacity with the same exception as under existing law; (c) specifying that a beneficiary may disenroll on a monthly basis with one month's notice; and (d) providing that a plan may not disenroll or refuse to reenroll a beneficiary because of health status or services required.

The Senate amendment would specify that 50 percent of enrollees must be other than medicare or medicaid beneficiaries, however, the Secretary could waive this requirement. In no case could more than 50 percent of enrollees be medicare beneficiaries. The Secretary would be required to establish minimum standards for consumer information to be supplied to eligible beneficiaries.

The Senate amendment would specify that reasonable cost reimbursement be available indefinitely. Under the risk reimbursement contract, the calculation of the Government's contribution would be based on 95 percent of the AAPCC (including certain administrative costs), reflecting such factors as age, sex, institutional status, disability and health status, and place of residence. Plans with at least 1,000 members would be eligible for risk contracts.

The Senate provision would require three new medicare members to enroll in a plan for every current medicare enrollee allowed to convert to the new reimbursement system and that current HMO enrollees turning age 65 would be included in the formula.

The Senate provision would provide that if the adjusted community rate (ACR) for a plan is less than the AAPCC, the plan must spend the difference to provide additional benefits or services; reduction in premiums, deductibles, or copayments; or to provide rebates and dividends to the enrollees. Further, a committee of medicare enrollees must approve the additional benefits.

House committee provision

The House committee provision would authorize a medicare payment option for health maintenance organizations (HMO's). The provision is similar to the Senate amendment except: State licensed HMO's are not included in the definition of an eligible HMO; the length of the annual open enrollment period is to be of "reasonable duration"; services must be accessible to enrollees within the HMO service area; rebates and dividends would not be permitted; two new medicare members must enroll in a plan for every current medicare enrollee allowed to convert under the risk contract; and additional non-optional services would have to be approved by the Secretary.

Conference agreement

The conference agreement follows the Senate amendment with modifications. The agreement authorizes both prospective reimbursement under risk-sharing contracts and cost-based reimbursement under reasonable cost reimbursement contracts for health maintenance organizations (HMO's) and other medical plans. It contains compromise language permitting the Secretary to enter into risk-sharing contracts with eligible organizations which have at least 5,000 members, although this limitation may be waived for plans in non-urbanized areas. The Secretary may enter into reasonable cost reimbursement contracts with eligible organizations which he or she determines do not have the capacity to bear the risk of potential losses under a risk-sharing contract or which so elect or which do not meet the membership size limitation.

The conference agreement defines organizations eligible to enter into contracts under section 1876 as federally qualified HMO's, or HMO's or other plans meeting a generic definition of comprehensive health plans. The Senate amendment regarding State licensed HMO's was not included. The additional requirements with respect to the provision of services to medicare members combine the similar Senate and House committee requirements and include the Senate requirement that the annual open enrollment period must be of at least 30 days duration. As provided in the Senate amendment, an HMO's or plans combined medicare and medicaid enrollment cannot exceed 50 percent except under certain circumstances where a waiver is available.

The conference agreement includes language similar to the Senate amendment describing the actuarial factors to be used in setting the amount of the prospective medicare payment under a risk-sharing contract. In making the adjustment for disability status the Secretary can use his or her discretion as to whether to take into account eligibility for cash payments under the disability insurance program or under SSI.

The conference agreement provides that, as in the House committee provisions, to the extent that the medicare payment exceeds the eligible organization's adjusted community rate under a risk-sharing contract, the organization must use the savings to provide its medicare members with additional health benefits or reduced cost sharing. The Senate amendment permitting rebates and dividends was not included. The Senate amendment requiring that a group of the organization's medicare members must select any additional benefits was also not included, and the House committee language permitting the organization to decide upon the use of the savings was included.

The conference agreement contains the House committee language requiring two new medicare enrollees to enroll for every one current medicare member who converts to the new system under a risk-sharing contract.

The conference agreement retains the identical Senate amendment and House committee language regarding the effective date.

The conferees have agreed upon this delay in implementing this new reimbursement system because of their concern that the adjustments made under the current AAPCC do not adequately reflect the relative health care needs (i.e., disability status and other characteristics) of medicare beneficiaries who enroll in the HMO as compared to beneficiaries in the fee-for-service system. The Secretary must develop additional adjustment factors to account for the resulting cost differentials before implementing the program.

Conference agreement

The conference agreement includes the Senate amendment.

22. Hospice care

Senate amendment

The Senate amendment authorizes coverage under medicare part A for hospice care for terminally ill beneficiaries with a life expectancy of six months or less. A medicare beneficiary could elect to receive hospice care in lieu of other medicare benefits except those of the attending physician. Benefits covered include nursing care, therapies, medical social services, homemaker-home health aide services, short-term inpatient care, outpatient drugs for pain relief and respite care. The provision requires that hospices be classified as a separate provider category in the medicare program. Reimbursement would be based on reasonable costs or such other test of reasonableness as the Secretary shall determine, subject to an area adjusted limit or cap set at 40 percent of the average medicare per capita expenditure during the last six months of life for medicare beneficiaries dying of cancer. The provision requires the Secretary to continue the existing Health Care Financing Administration's hospice demonstration projects until the effective date of the hospice benefit. Special exceptions are provided for certain well established hospices.

House committee provision

The House committee provision includes a similar provision.

Conference agreement

The conference agreement follows the Senate amendment with modifications: The benefit period would consist of two periods of 90 days and one period of 30 days; the reference to "speech therapy" would be changed to "speech-language pathology"; copayments would be limited to approximately (i) 5 percent of a hospices cost (as determined by the Secretary) for respite care services, but such coinsurance amount could not exceed the inpatient hospital deductible during a hospice election (as long as the hospice election is not broken by more than 14 days); (ii) in addition, copayments equal to the lesser of, approximately 5 percent of charges or $5 per prescription, for covered drugs; no reimbursement would be permitted under part B of medicare for an individual's attending physician if the attending physician is employed by the hospice; a hospice program would have to provide directly substantially all of the following core services; nursing care provided by or under the supervision of a registered professional nurse, medical social services under the direction of a physician, physicians services and counseling services; the amendment would be clarified to provide that non-core services, including physical and occupational therapy, speech-language pathology, home health aide services and homemaker services, medical supplies and inpatient services could be provided "under arrangements" with others; the written plan of care could be reviewed by the attending physician as well as the hospice physician.

The Senate amendment would be clarified to authorize the Secretary to eliminate duplication where any provider requirements under this provision are the same as requirements already met by the provider under other agreements with the Secretary. In addition the Secretary is required to coordinate surveys for determining certification under this title so as to provide, to the extent feasible, for simultaneous surveys of an entity which seeks to be certified as a hospice program and as a provider of services of another type. Hospice would be required to file separate cost reports.

It is the intent of the conferees that hospices provide a basic and coordinated range of services while giving hospices the flexibility to provide, under arrangements, for some services. Hospices would not be required to provide inpatient services directly. However, it is the intention of the conferees that the hospice would be directly responsible for: providing professional supervision over care provided in the inpatient unit; for ensuring that the care provided in the inpatient unit be consistent with the hospice concept of care through the delivery of care or supervision of such care by an interdisciplinary group; and, that the treatment provided be reasonable and necessary for the palliation and management of terminal illness.

Counseling services would be required as a core service under the hospice benefit. The conferees understand that counseling services are an integral part of hospice care however, concern has been expressed regarding the potential cost impact of allowing separate billing for such services. The conferees intention is to permit reimbursement for the salaries of counselors but not to provide reimbursement for services billed as a separate service.

The conferees provided an exception for hospices which commenced operation before January 1, 1975 from; (i) the reimbursement cap; (ii) the limitation on inpatient days; and (iii) the limitation on respite care days. In allowing the above exceptions for these earliest of the Nation's hospices, the conferees intend to give them an opportunity to conform to the prevailing patterns of hospice care and to meet the requirements in the law. The conferees anticipate that no extension of the exemption would be allowed after November 1, 1986, should the basic hospice provision be extended beyond that date.

The provision would be effective for hospice care provided on or after November 1, 1983. The provision would sunset on October 1, 1986, however, an individual who has an election in effect for a period on October 1, 1986, is entitled to hospice care benefits after that date for the remainder of that period and for any subsequent consecutive period to which the individual would have been entitled before such date.

23. Coverage of extended care services without regard to 3-day prior hospitalization requirement

Senate amendment

No provision.

House committee provision

The House committee provision directs the Secretary to provide skilled nursing facility coverage without regard to the 3-day prior hospital stay requirement at such time as, through reimbursement changes or other adjustments, the Secretary determines that this will not lead to an increase in cost and will not alter the acute care nature of the benefit. For persons covered without a prior hospital stay, limitations may be provided on scope or extent of services and on categories of individuals eligible.

Conference agreement

The conference agreement includes the House committee provision.

24. Prohibiting recognition of payments under certain percentage arrangements

Senate amendment

No provision.

House committee provision

Under the House committee provision, no cost which a provider incurs under a contract would be considered reasonable if determined as a percentage (or other proportion) of the provider's reimbursement or claim for reimbursement for services. The provision would not apply to a percentage contract that is reasonable and where such contract is a customary commercial business practice (e.g. commissions paid to salesmen) or provides incentives for the efficient and economical operation of the provider of services.

The provision would generally apply upon enactment. However, for arrangements entered into before enactment, the provision applies one year after enactment, except where provider can unilaterally terminate the arrangement, in which case the provision applies 30 days after the first date that the provider can terminate the arrangement.

Conference agreement

The conference agreement includes the House committee provision with modifications. The prohibition would apply to contracts where the cost is determined on the basis of a percentage (or other proportion) of the provider's charges, revenues, or claim for reimbursement. The provision would be effective upon enactment with certain exceptions as in the House committee provision. The provision would not apply prior to October 1, 1982 to costs incurred under a percentage arrangement where such costs were attributable to the services of a provider-based physician (described in Item 8 of the conference agreement). Beginning October 1, 1982, the provision would not apply to such a provider-based physician where the limitation on reimbursement for the cost of such a physician's services had been implemented.

25. Interest charges on overpayments and underpayments

Senate amendment

No provision.

House committee provision

The House committee provision requires that once a final determination is made that a provider or supplier has received an overpayment or underpayment from medicare, and payment of the excess or deficit is not made within 30 days of the date of determination, interest charges would be applied to the balance due.

The rate of interest charged would equal the average of the rates of interest on obligations issued for purchase by the Federal Hospital Insurance Trust Fund for the 3-month period ending with the month before the month in which the final determination is made. The provision would be effective with respect to final determinations made on or after the date of enactment.

Conference agreement

The conference agreement follows the House committee provision with a modification providing that interest would be determined in accordance with regulations of the Secretary of the Treasury applicable to charges for late payments which are periodically published pursuant to Section 8020.20 of the Treasury Fiscal Requirements Manual.

26. Prohibiting payment for Hill-Burton free care

Senate amendment

No provision.

House committee provision

The House committee provision requires the Secretary to provide, by regulation, that the costs incurred by a hospital or skilled nursing facility in complying with its free care obligation under the Hill-Burton Act would not be considered reasonable costs for purposes of medicare reimbursement. The provision is effective for costs incurred on or after date of enactment.

Conference agreement

The conference agreement includes the House committee provision. The provision is intended to clarify that Hill-Burton free care costs have never been, and are not, allowable for medicare reimbursement purposes. The provision, therefore, applies to all such costs that have been, or will be incurred except those recognized by the final judgment of a U.S. Court of Appeals entered into prior to enactment.

27. Prohibiting payment for anti-unionization activities

Senate provision

No provision.

House committee provision

The House committee provision prohibits medicare reimbursement for costs incurred for activities directly related to influencing employees with respect to unionization. The provision would apply to costs incurred on or after date of enactment.

Conference agreement

The conference agreement includes the House committee provision.

28. Eliminating "lesser of cost or charges" provision

Senate amendment

No provision.

House committee provision

The House committee provision specifies that the lesser of cost or charges provision would not apply to a class of providers if the Secretary determines and certifies to the Congress that its elimination will not increase medicare payments to that class of provider. It is intent of the conferees that such a determination would take account of both past experience under the provision and possible changes in the cost accounting and charging practices of providers in the absence of the provision.

The provision would be effective on the date the Secretary specifies in his certification to Congress.

Conference agreement

The conference agreement includes the House committee provision. It is the intent of the conferees that the lesser of cost or charges provision be reestablished at such time as the Secretary determines that the non-application of the provision has increased program costs.

29. Extending medicare proficiency examination authority

Senate amendment

No provision.

House committee provision

The House committee provision extends to September 30, 1983, the period during which the Secretary shall conduct a program to determine the proficiency of health care personnel, including clinical laboratory personnel, who do not meet formal education requirements. The provision would be effective upon enactment.

Conference agreement

The conference agreement includes the House committee provision.

30. Prohibiting retroactivity of regulations regarding access to books and records

Senate amendment

No provision.

House committee provision

The House committee provision would prohibit regulations yet to be issued under the authority of section 952 of Public Law 96-499, the Omnibus Budget Reconciliation Act of 1980, from being applied retroactively.

Section 952 of Public Law 95-499 requires the Secretary of HHS or the Comptroller General to have access to the books and records of subcontractors who supply providers with goods and services valued at $10,000 or more over a 12-month period. The law directs the Secretary to prescribe in regulations the procedures and criteria to be used in obtaining access to such books and records.

The provision would become effective upon enactment.

Conference agreement

The conference agreement includes the House committee provision, with a modification which would prohibit the regulations from being applied retroactively unless such regulations are issued in final form prior to January 1, 1983, preceded by a comment period of no less than 60 days.

31. Health Care Financing Administration/private sector utilization review initiative

Senate amendment

No provision.

House bill

No provision.

Conference agreement

Under the conference agreement, the Secretary of HHS would be required by statute to undertake an initiative to improve medical review by intermediaries and carriers under Title XVIII of the Social Security Act and to encourage similar review efforts and utilization control activities by private insurers and other private entities. The medicare initiatives shall include the development of fiscal targets and evaluation of the performance of intermediaries and carriers with respect to the identification and reduction of unnecessary utilization of health services.

It is the intent of the conferees that, where such review activity results in denial of payment to institutional and other providers under medicare, such providers shall be prohibited from collecting any payments from beneficiaries (in excess of those otherwise provided for under current medicare law.)

32. Special part B enrollment without penalty (Merchant Seamen)

Senate amendment

No provision.

House committee provision

The House committee provision establishes a special enrollment period for medicare part B beginning on the first day of the first month beginning at least 20 days following enactment, and ending on December 31, 1982. During that period, otherwise eligible merchant seamen and other individuals would have a one-time opportunity to enroll in part B without incurring the current law penalty of higher premium payments for delayed enrollment.

Conference agreement

The conference agreement includes the House committee provision, modified to provide the special open enrollment period for merchant seamen only.

SUBTITLE B—MEDICAID PROVISIONS

1. Copayments by medicaid recipients

Senate amendment

The Senate amendment permits States to impose nominal copayments on all beneficiaries for all services with certain exceptions. The Senate provision provides for the following limitations on copayments:

(a) Precludes States from imposing such charges with respect to inpatient hospital services and mandatory ambulatory services for categorically needy children under 18 and services related to the pregnancy of categorically needy women, and permits States similarly to exclude medically needy children and pregnant women from copayments.

(b) Precludes States from imposing copayments with respect to all services provided to categorically needy SNF/ICF patients; permits States to exempt medically needy SNF/ICF patients from copayments.

(c) Precludes States from imposing copayments on emergency services for categorically needy persons.

(d) Permits States to exempt all HMO enrollees from copayments.

The provision would be effective on enactment.

House committee provision

The House Committee provision permits States to impose nominal copayments on all beneficiaries for all services with certain exceptions. The provision specifies a $1 maximum allowable copayment amount for hospital, physician, outpatient, and clinic services for the categorically needy; copayments of up to $4 would be allowed for non-emergency services in emergency rooms.

The provision also provides for the following limitations on copayments:

(a) Precludes States from imposing charges with respect to all services for categorically needy and medically needy pregnant women and children under 21.

(b) Precludes States from imposing copayments with respect to all services provided to categorically needy SNF/ICF patients.

(c) Precludes States from imposing copayments on emergency services for categorically needy and medically needy persons.

(d) Precludes States from imposing copayments on categorically needy recipients enrolled in an HMO.

(e) Precludes States from imposing copayments on family planning services.

The House provision would be effective October 1, 1982.

Conference agreement

The conference agreement is similar to the Senate provision with modifications. The conference agreement specifies, with one exception, that all copayments must be nominal in amount. The conferees intend that the existing regulations defining "nominal" will continue to serve as the basis for determining whether proposed copayment charges meet the statutory requirements. If the Secretary determines in the future that adjustments to the current regulations are to be made, it is the intention of the conferees that the levels of cash assistance in the States should be considered. The conferees recognize that persons depending on cash assistance have little available income to make copayments, and the standards for nominality should be such that the copayments do not serve as a barrier to receipt of necesssary medical services. The conferees intend that the Secretary, in promulgating regulations implementing this provision, adhere to the requirements for notice and opportunity for comment under the Administrative Procedures Act, 5 U.S.C. 553(a)(2), including the issuance of a notice of proposed rulemaking. The Secretary may not redelegate the definition of "nominality" to the States.

The "nominal" requirement cannot be waived except for demonstration under tightly limited circumstances, with one exception. The Secretary could waive the requirement limiting copayments to nominal amounts in the case of nonemergency services in emergency rooms where the State has established to the satisfaction of the Secretary that alternative sources of nonemergency outpatient services are actually available and accessible. Where the Secretary is satisfied that such conditions have been met, and a waiver has been granted, the State may impose a charge up to twice the amount defined as nominal by the Secretary in regulations.

The conference agreement precludes States from imposing copayments on children under age 18; States may provide that no copayments would be imposed for children aged 18 to 21. The agreement also precludes States from imposing copayments on services related to pregnancy (including prenatal, delivery, and post partum services). States may at their option provide that no copayments would be imposed for any service provided to pregnant women. These limitations would apply to both categorically needy and medically needy persons.

The conference agreement bars States from imposing copayments on all services provided to inpatients in SNF's and ICF's who are required to spend all their income for medical expenses except for the amount exempted under the State standard for personal needs (which cannot be less than the SSI payment for persons in medical institutions, and which may be more). This prohibition on copayments also extends both to the categorically needy and medically needy population groups.

The conference agreement bars States from imposing copayments on categorically needy HMO enrollees. States may also exempt medically needy HMO enrollees from such charges.

With these exceptions, the conference agreement makes no changes in the comparability requirements of current law.

Additionally, the agreement provides that copayments may not be imposed on family planning services or emergency services for either categorically needy or medically needy individuals.

The conference agreement is designed to allow States to deter unnecessary utilization while not imposing an unreasonable hardship on beneficiaries. The conference agreement therefore includes a provision which specifies that no provider participating under medicaid may deny care or services to an individual because of his or her inability to pay the required cost-sharing charges. This does not excuse the beneficiary from liability for paying such charges.

2. Elimination of Federal matching for medicare part B buy-in

Senate amendment

The Senate amendment eliminates Federal matching for all medicare part B premium payments. Most State medicaid plans currently make the monthly medicare part B premium payment for their dual eligible beneficiaries under a "buy-in" agreement. Federal matching for premium payments is only available for the cash assistance groups.

The provision is effective with respect to premiums due for months after September 1982.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate provision.

3. Modifications in Lien Provision

(A) LIENS

Senate amendment

The Senate amendment allows States to impose liens on the real property, including the home, of institutionalized medicaid recipients who fail to make a showing that they reasonably expect to be discharged from a nursing home or other long-term medical institution and return home.

The Senate amendment specifies that the lien could not be foreclosed (and States could not recover the cost of medical assistance provided) until the recipient voluntarily chooses to sell the property, or, until after the recipient's death, and the death of the surviving spouse and/or any children who are under 21, blind or disabled.

House committee provision

The House Committee provision allows States to impose liens on real property, including the home, of institutionalized medicaid recipients who the State establishes are reasonably likely to remain in a nursing home for the remainder of their lives.

The House Committee provision is similar to the Senate provision with respect to allowable foreclosure actions. However, it specifies that the State could also not execute a lien while a recipient's sibling, son, or daughter is lawfully residing in the home and was living in the home for at least one year immediately prior to the recipient's admission to the nursing home. Further, if the home is sold before the lien is executed, the proceeds would be put in trust and used to meet the support needs of the spouse and minor or disabled child.

Conference agreement

The conference agreement follows the Senate amendment with modifications. States are allowed to impose liens on real property, including the home, of institutionalized medicaid beneficiaries who the State determines, after notice and opportunity for a hearing, are reasonably likely to remain in a nursing home for the remainder of their lives. The burden of proof in this determination, which is to be conducted in accordance with procedures established by the State, is on the State. States are not authorized to impose liens on the homes of beneficiaries if the spouse, or blind, disabled or dependent child is residing in the home, or if a beneficiary's sibling is residing in the home who has equity in the home and who has lived there continuously since at least one year prior to the beneficiary's admission to the nursing home.

The agreement further specifies that while a State may impose a lien, it may not foreclose upon the property while a beneficiary's adult son or daughter is residing in the home if he or she (1) has lived in the home continuously for at least two years prior to the beneficiary's admission to the nursing home; and (2) has provided care to the beneficiary that permitted the individual to delay institutionalization; or if a sibling, even though without equity in the home, has lived there continuously since at least one year prior to the beneficiary's institutionalization.

(B) TRANSFER OF ASSETS

Senate amendment

The Senate amendment allows States to deny medicaid eligibility for 24 months and (at State option) for a longer period to persons who dispose of their homes for less than fair market value, within 24 months prior to admission to an institution even though such disposal would not make them ineligible for SSI.

States could either deny eligibility to all such individuals for periods reasonably related to the uncompensated value, or they could deny eligibility in all cases for a minimum of 24 months, with the option to provide for longer periods of ineligibility in the case of individuals who disposed of homes worth substantial amounts. The provision would not apply in the case of individuals who reasonably expected to be discharged from the medical institution and return home; individuals who demonstrated that they had intended to obtain fair market value or other valuable consideration in exchange for their homes; or individuals who transferred title to their homes to a spouse or a minor or handicapped child. The State could also make an exception in other cases where undue hardship would otherwise result.

House committee provision

The House Committee provision is similar to the Senate amendment. However, the provision applies to transfers for less than fair market value within 24 months prior to application for benefits. In addition, the provision allows States to deny medicaid coverage for a period computed in a manner such that the cost of the services that would otherwise be provided to the individual during this period bears a reasonable relationship to the amount of the uncompensated value of the home. The period of ineligibility would begin with the month in which the home was disposed of.

Conference agreement

The conference agreement follows the Senate amendment with modifications to specify that the period of ineligibility is 24 months from the date of transfer, except that States: (a) are allowed to deny eligibility for a longer period if the uncompensated value of the home is greater than the cost of 24 months of medicaid benefits; and (b) are required to set a shorter time period if the uncompensated value of the home is less than 24 months of medicaid benefits. Under either circumstance, the period of eligibility delay must be related to the uncompensated value of the home, based on the beneficiary's equity, and the cost of medicaid benefits. The provision applies to transfers for less than fair market value occurring up to 24 months prior to application for medicaid benefits.

The conference agreement also amends existing law transfer of assets policy by allowing a State to waive the delay of medicaid eligibility in cases of undue hardship. The conferees also note that the change in SSI policy which exempts burial spaces and certain policies from an individual's resources (see item No. 6 of Subtitle F) has the effect of also exempting such items from an individual's resources for purposes of determining medicaid eligibility in most States.

(C) EFFECTIVE DATE

Senate amendment

The Senate amendment is effective on enactment.

House committee provision

The House Committee provision applies to applications for assistance filed on or after October 1, 1982.

Conference agreement

The conference agreement specifies enactment as the effective date for the lien provisions and specifies that the provision applies with respect to transfers of assets occurring after the date of enactment.

4. Limitation on Federal financial participation in erroneous medical assistance expenditures

Senate amendment

The Senate amendment deletes the Medicaid error rate provisions and penalties incorporated in the 1980 Appropriations Act and substitutes language establishing a 3 percent target error rate for quarters beginning after March 30, 1983. The provision provides that prospective fiscal sanctions are to be applied beginning in the second half of FY83 for States which have error rates exceeding 3 percent. The Secretary is provided discretion in applying the fiscal penalties, in whole or in part, for a State which has made good faith efforts to meet the target. The provision is effective on enactment.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate provision with modifications. Technical errors, i.e., errors which if corrected would not have made a difference in the amount of medical assistance paid, would be excluded from the calculation. The agreement specifies that where errors are made relating to amounts of medical expenses that must be incurred to establish Medicaid eligibility (the "spend-down" requirement), only the smaller of the amount of medical assistance provided or the amount of the spend-down that was miscalculated shall be determined to be an erroneous payment. Further, errors in determination of resources are treated in a similar manner: only the smaller of the amount of medical assistance provided or the amount of miscalculation of the resource which exceeded the allowable resource level will be counted as an erroneous payment.

5. Optional medicaid coverage for individuals who would have qualified for AFDC but for amendments to the earned income disregard and related provisions

Senate amendment

The Senate amendment allows States to continue medicaid coverage for working families who are made ineligible for AFDC as a result of certain changes made by the Omnibus Budget Reconciliation Act of 1981. (Public Law 97-35). These changes, relating to the earned income disregard and work expense deductions, resulted in the loss of AFDC eligibility, and therefore automatic medicaid coverage, for certain individuals. The amendment would be effective for calendar quarters beginning after the date of enactment.

House committee provision

Similar provision.

Conference agreement

The conference agreement does not contain the Senate amendment or the House Committee provision.

6. Medicaid coverage of home care of certain disabled children

Senate amendment

No provision.

House committee provision

The House committee provision provides States with the option of covering under Medicaid certain disabled children age 18 or under who are living at home. A State could extend such protection to an individual who would be eligible for SSI, and therefore Medicaid, if he was in a medical institution. Further, the State must determine that: (a) the child requires the level of care provided in an institution; (b) it is appropriate to provide such care outside of the institution; and (c) the estimated cost of care at home is no more expensive than the estimated cost of institutional care.

Conference agreement

The conference agreement includes the House committee provision.

7. Technical corrections relating to medicaid

Senate amendment

The Senate amendment makes technical changes in Public Law 97-35.

House committee provision

The House committee provision includes identical technical changes with one additional provision specifying that the Secretary is not authorized to waive the requirements for State contracting on a risk basis with HMO's and other prepaid entities found in section 1903(m) of the Social Security Act.

Conference agreement

The conference agreement follows the Senate provision with a modification to delete the Secretary's authority to waive the section 1903(m) requirements. However, the conferees recognize that some waivers of section 1903(m) have already been granted. In order to minimize the disruption of arrangements which have already been implemented under these waivers, the conference agreement specifies that the limitation on the Secretary's waiver authority shall not apply where a waiver was granted by the Secretary and the waivered arrangements were in effect prior to August 10, 1982. This exemption extends only for the period for which the waiver was initially approved.

It is understanding of the conferees that the types of entities subject to the requirements of section 1903(m) would not include contractual arrangements between the State and an individual physician, or a group of physicians, under which (1) case management is the primary purpose; (2) hospital services are not provided directly by, or under contract for payment to, such physician or physician group; (3) the physician or physician group receives at least 25% of its gross revenues from non-Medicaid and non-Medicare patients (through fee-for-service or other reimbursement methods); (4) the Medicaid revenues that the physician or physician group would otherwise receive from the arrangement will not increase more than 20% as a result of a decrease in the use by beneficiaries under management of hospital and other covered services; and (5) primary care services are available on a 24-hour basis.

The conference agreement makes explicit current law related to coverage of the optional categorically needy, as reflected in current regulations at 42 CFR § 435.210 *et seq.* The conferees do not intend any change in current law through this recodification.

8. Medicaid funding in American Samoa

Senate amendment

No provision.

House bill

No provision.

Conference agreement

The conferees agreed to a provision providing medicaid funding to the territory of American Samoa. Federal matching of 50 percent of expenditures would be authorized, up to a maximum Federal contribution of $750,000 per year. Due to the unique circumstances in the health system in American Samoa, the Secretary is authorized to waive any provisions of title XIX except the requirements (1) of State matching, (2) of the maximum amount of Federal funds that can be spent, and (3) that expenditures be for health services covered under the title.

9. Nursing home deregulation moratorium

Senate amendment

No provision.

House committee provision

No provision.

Conference agreement

The conferees agreed to a provision which would preclude the Department of Health and Human Services from implementing certain proposed changes regarding survey and certification requirements for nursing homes for 6 months from the date of enactment of this provision. The intent of the conferees in establishing this moratorium is to provide opportunity for the further review, revision or withdrawal of the proposed regulations, published in the Federal Register on May 27, 1982. The conferees anticipate that the Secretary would consult with the Congress, the General Accounting Office, groups representing nursing home residents, state survey and certification agencies and nursing home operators prior to resubmitting the regulations. The conferees do not intend to preclude courts with proper jurisdiction from ordering changes in the current regulations prior to the end of the moratorium.

SUBTITLE C—UTILIZATION AND QUALITY CONTROL PEER REVIEW

1. Establishment of utilization and quality control peer review program

Senate amendment

The Senate amendment repeals the existing Professional Standards Review Organization (PSRO) program and requires the Secretary to enter into contracts for utilization and quality control peer review. The Secretary would also be required to consolidate geographic areas previously established for PSRO's.

The provision requires the Secretary to enter into contracts with peer review organizations for an initial period of 2 years, renewable biennially. The organizations must be composed of, or have available to them, a substantial number of licensed doctors of medicine or osteopathy actually practicing in the area. Priority consideration must be given to physician-sponsored organizations who are representative of the physicians in the area. Payor and provider organizations would be excluded from consideration during the first 12 months that contract applications are considered.

Review organizations, which can be proprietary or nonprofit, may review the professional activities of physicians, other practitioners and institutional and noninstitutional providers in providing services to medicare beneficiaries subject to the provisions of these contracts. The review will focus on (1) the necessity and reasonableness of care, (2) quality of care, and (3) the appropriateness of the setting.

House bill

No provision.

Conference agreement

The conference agreement follows, with modifications, the Senate provision repealing the existing Professional Standards Review Organization (PSRO) program and requiring the Secretary of HHS to enter into performance contracts for utilization and quality control peer review.

The conference agreement follows the Senate amendment requiring the Secretary to consolidate existing PSRO review areas. The conferees intend that the Secretary, in consolidating review areas, shall maximize administrative and review efficiency. The conferees intend that the Secretary will not teminate small PSRO's that are operating effectively and efficiently but will instead permit such PSRO's to contract with the new review organization for that area without duplication of administrative costs.

The conference agreement follows the Senate amendment regarding the conclusiveness of determinations respecting payment. It is the understanding of the conferees that, where such review activity results in denial of payment to institutional or other providers under medicare, such providers will be, as under current law, prohibited from collecting any payments from beneficiaries in excess of those otherwise provided for under current medicare law.

The conference agreement follows the Senate amendment requiring 2-year contracts with peer review organizations composed of, or having available, a substantial number of licensed physicians with a modification which would:

(a) prohibit contracts with provider or provider-affiliated organizations (although subcontracts for delegated review purposes with such organizations would be permittted) and

(b) provide that contract termination procedures would not apply to contract nonrenewals.

The conferees intend that review organizations avoid financial conflicts of interest with providers subject to review. The conference agreement prohibits the Secretary from entering into a contract with an entity which is, or is affiliated through management, ownership, or common control with, a health care facility or association of such facilities whose services they would be responsible for reviewing. The conference agreement does not, however, bar a review organization from delegating the review function to a provider by subcontract, if the organization finds that the provider will effectively and efficiently review itself.

The conference agreement follows the Senate provision exempting review organizations from the Freedom of Information Act and establishing disclosure rules for such organizations that apply uniformly to both public and private review activities undertaken by the organizations, with a modification which would:

(a) require the review organization to disclose to the appropriate State agency information identifying a particular practitioner or provider when, in the organization's judgment, there is a reason to believe that a risk to the public health exists, and

(b) require the review organization to disclose information to a State or Federal fraud or abuse agency or an authorized State licensure or certification agency, but only at the request of such agency on a case-by-case basis. This information could include institution or practitioner-specific data.

The conference agreement follows the Senate provision relating to the transition from the existing PSRO program with a modification which would prohibit the Secretary from terminating a PSRO in effect on the earlier of September 30, 1982 or enactment, until such time as the Secretary has entered into a contract with a review organization in that area under this provision.

The conference agreement follows the Senate provision requiring the Secretary to report to the Congress annually with a modification requiring the Secretary to provide information on the efficiency of payment methodologies used by the Secretary in contracting with review organizations.

SUBTITLE D—AID TO FAMILIES WITH DEPENDENT CHILDREN

1. Rounding of eligibility and benefit amounts

Senate amendment

The Senate amendment requires States to round both their AFDC need standard and actual monthly benefit amounts to the next lower whole dollar. The provision is effective October 1, 1982, or later if State conforming legislation is needed.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

2. Effective date of application; proration of first month's benefit

Senate amendment

The Senate amendment prohibits States from making benefits payable for any period prior to the date an application is filed. Any payment for the first month of eligibility would be prorated based on the date of the application. The provision is effective October 1, 1982, or later if State conforming legislation is needed.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

3. Absence from home solely by reason of uniformed service

Senate amendment

Under the Senate amendment, AFDC would no longer be payable to families if the parent is absent solely because of active duty in the uniformed service. The provision is effective October 1, 1982, or later if State conforming legislation is needed.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

4. Sanction for termination or reduction of employment.

Senate amendment

The Senate amendment provides the Secretary of Health and Human Services authority to prescribe sanctions for individuals who are exempt from registration for the work incentive (WIN) program because they are employed 30 or more hours a week, or who live in an area so remote from a WIN program that their participation is precluded if they refuse a bona fide offer of employment, terminate employment, or reduce their hours of employment, without good cause.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

5. Job search

Senate amendment

The Senate amendment requires State welfare agencies to establish mandatory employment search programs for both applicants and recipients of AFDC. An individual who is required to register for WIN (or who would be required to register except for remoteness from a WIN site) would be required to participate beginning at the time of application. The individual would also be required annually to participate in a program of employment search after his application becomes effective whenever the State prescribes, but not more than a total of 8 weeks in each year. An individual who fails to comply with the employment search requirement, would be subject to sanctions in the same manner as under the WIN program. (The WIN sanctions provide that in the case of the principal earner in an unemployed parent family, the sanction is denial of benefits for the entire family. In other cases, the individual who refuses is removed from the grant and the family's benefit is reduced. The sanction period is 3 months in the case of a first refusal and 6 months in the case of any subsequent refusals.)

House committee provision

The committee provision differs from the Senate amendment as follows:

(1) It is optional with the States.

(2) It allows States to limit participation to certain groups or classes of individuals who are required to register for WIN.

(3) It allows the State to shorten the duration of the sanction period.

(4) It includes a provision which specifically requires payment to the individual of transportation and other costs necessarily incurred.

(5) It provides 50 percent Federal matching for costs of transportation and other necessary services.

(6) It prohibits States from using the job search requirement as a reason for any delay in making a determination of an individual's eligibility or in issuing a payment to an individual who is otherwise eligible.

(7) It allows an initial 8-week search period, and an additional 8-week period each year (which could add up to 16 weeks in the first year).

Conference agreement

The conference agreement follows the House committee provision, but with the Senate effective date of October 1, 1982.

6. Inclusion and exclusion of specified individuals' needs and income

(A) ELIGIBILITY OF A PARENT

Senate amendment

In determining the AFDC benefit, States are currently permitted to include the needs of a parent or caretaker relative so long as the youngest child is under age 18 (or, at State option, under 19 if the child is in school and is expected to complete his course of study before reaching his 19th birthday). The Senate amendment requires States to include the needs of a parent or caretaker relative, but only until the youngest child reaches age 16. The income and resources of the ineligible parent would be counted in determining the benefit for the child. The State would continue to include the need of a parent of an older eligible child if the parent is unemployable.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

(B) INCLUDE ALL SIBLINGS IN THE AFDC UNIT

Senate amendment

Currently, an AFDC family may choose to exclude a child from the assistance unit if that child has income which would reduce the amount of the family's benefit. The Senate amendment requires States to include all children in the family unit (except disabled children receiving SSI benefits, and certain stepbrothers and stepsisters) in determining the amount of AFDC for which the family is eligible.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

(C) COUNTING INCOME OF GRANDPARENTS

Senate amendment

Currently, the income of parents of a minor child, who is herself the parent of a child, is not counted in determining the eligibility and benefit of the grandchild. The Senate amendment requires States, when the AFDC parent is a minor, to count the income of the grandparents who are living in the same household as available to the grandchild, after setting aside certain amounts to cover their own needs. The AFDC payment would be made to the grandparent.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

(D) COUNTING INCOME OF UNRELATED INDIVIDUALS

Senate amendment

Under current law, the income of an unrelated adult in an AFDC household may not be presumed to be available to the household, and the welfare agency may count only actual contributions which it knows have been made by the individual to the AFDC family. The Senate amendment requires States to count the income of any person living with the child who is not related to the child or parent or to any other individual living in the household. The income of the unrelated individual would be considered available to the AFDC family, after setting aside certain amounts to cover the needs of the unrelated person and any dependents.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

7. Repeal of emergency assistance program

Senate amendment

The emergency assistance program provides 50 percent matching for emergency assistance (in the form of cash, medical care, or services) to families with children, including both AFDC and non-AFDC families. Assistance may be provided for no more than 30 days in any 12 month period. The program is optional with the States. Under the Senate amendment, this program would be repealed, effective October 1, 1982.

House bill

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

8. Proration of standard amount for shelter and utilities

Senate amendment

AFDC regulations generally prohibit the States from prorating or otherwise reducing the AFDC benefit solely because of the presence in the household of an individual who is not legally responsible to support the family. This general prohibition was modified in Public Law 96-272 to allow States to prorate the shelter and utilities portion of the AFDC benefit in the case of "child only" family units, i.e., when the caretaker is not eligible for assistance.

The Senate amendment allows States to prorate the portion of the AFDC grant for shelter and utilities whenever the assistance unit shares the household with other individuals. The amendment gives States flexibility in determining how the proration provision would be applied. It requires that proration be accomplished "on a reasonable basis," and in a manner and under circumstances prescribed by the State. States could not prorate in the case of a recipient of Supplemental Security Income benefits to whom the one-third reduction applies. (The one-third reduction in the SSI benefit occurs when individuals are determined to be living in the household of another and receiving in-kind income in the form of food and shelter.) The effective date is October 1, 1982.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

9. Limitation on Federal financial participation in erroneous assistance expenditures

Senate amendment

Under current law, the "Michel amendment" requires States to reduce their AFDC payment error rate to 4 percent by September 30, 1982. Regulations require the States to achieve one-third progress toward the 4-percent payment error rate (measured from their error rate for the base period April-September 1978) by September 30, 1980, and two-thirds progress by September 30, 1981. The 4-percent goal is the standard for all assessment periods after September 30, 1982. States may be sanctioned by being required to repay the Federal Government the Federal cost of improperly paid benefits, as determined by quality control surveys. The Secretary may waive sanctions where he determines, in certain limited cases, that a State is unable to reach the required reduction in a given year despite a good faith effort.

The amendment continues the 4-percent error rate tolerance level for fiscal year 1983 and reduces it to 3 percent for fiscal year 1984 and years thereafter. Until April 1, 1983, any sanctions would continue to be applied under the existing authority of the Michel amendment. Starting on that date a new sanction authority would be established, under which Federal payments to the States for AFDC matching will be reduced each quarter on a current basis to reflect the Secretary's estimates as to the error rate prevailing in the State program during that quarter. If the Secretary's estimates are incorrect appropriate adjustments would be made in subsequent grants. The present authority of the Secretary to waive the sanctions in limited cases where he finds that States have failed to meet the target error rates despite a good faith effort to do so would be continued.

House bill

No provision.

Conference agreement

The conference agreement includes the Senate provision which continues the 4-percent error rate tolerance level for fiscal year 1983 and reduces it to 3 percent for 1984 and years thereafter. However, the conference agreement does not include the provisions which would give the Secretary of HHS the authority to reduce Federal matching each quarter on a prospective basis to reflect his estimates as to the error rate estimated in the State program during that quarter.

10. Households headed by minor parents

Senate amendment

The Senate amendment provides that, in order to qualify for AFDC benefits, a minor parent and her child would have to reside in the home of the minor parent's own parent or guardian. This requirement would not apply where: the minor parent was married at the time of (or any time prior to) application for benefits; the minor parent has no parent or legal guardian who is living and whose whereabouts are known; the State agency determines that the health and safety of the minor parent or child would be seriously jeopardized if they lived in the same residence with the parent or legal guardian; or, the minor parent lived apart from the parent or legal guardian for a period of at least one year prior to the birth of the child.

House bill

No provision.

Conference agreement

The Senate recedes.

11. Exclusion from income of certain State payments

Senate amendment

A provision in the 1981 Reconciliation Act (P.L. 97-35) required States to determine AFDC benefits on the basis of the family's income in the preceding month. Under certain circumstances, payment may be determined on the basis of income in the second preceding month. This may be necessary, for example, when the payment date is in the first week of the month and the State needs time to process the monthly report of income which must be submitted by the recipient. In either case, States may wish to supplement the AFDC payment with a non-Federally matched State payment in certain situations—for example, when a family loses employment and suffers an immediate loss of income. Under present law, however, if the State decides to assist a family during a payment adjustment lag, any supplement which it pays to the family is counted as income for the purpose of computing the following month's AFDC check.

The Senate amendment allows States to compensate for payment adjustment lags by excluding from the calculation of AFDC benefit amounts any payments which are determined to have been paid by the State in recognition of the difference between the current or anticipated needs of the family for a month based upon actual income for the month, and the needs of the family as determined under the retrospective accounting procedure. The effective date is October 1, 1982.

House committee provision

The provision is the same (with technical differences).

Conference agreement

The conference agreement follows the Senate amendment.

12. Extension of time for States to establish a work incentive demonstration program

Senate amendment

The 1981 Reconciliation Act (P.L. 97-35) included a provision authorizing States to operate 3-year demonstration programs as alternatives to the current WIN program. The demonstration is aimed at testing single-agency administration and must be operated under the direction of the State welfare agency. The legislation required States to submit an application to the Secretary of HHS specifying intent to operate a WIN demonstration program. This application had to be submitted within 60 days after enactment.

The Senate amendment allows States a period of two additional years in which to exercise their option to operate a WIN demonstration program. This would give the States until June 30, 1984 to make this decision. The authority which the Secretary now has to waive requirements for participation in WIN would be extended to the demonstration programs. The provision is effective upon enactment.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

13. Exclusion from income

Senate amendment

No provision.

House committee provision

Under current law, income received by an AFDC household is generally counted as income in determining eligibility for and amount of assistance, unless specifically excluded. The Department of Health and Human Services has not in the past required that certain State payments be considered income for purposes of determining AFDC eligibility or amount of benefits. These are payments that are financed wholly from State funds to meet the needs of children receiving AFDC which are not met by the regular payment.

The committee provision allows States to continue to exclude from countable income, both in the month of receipt and in future months, certain special payments made by a State to AFDC households. To qualify for such an exclusion, the payments must have been originally authorized by State statute prior to January 1, 1979; be paid entirely from State funds by the State agency administering the AFDC program; and be provided to meet the needs of AFDC children. The effective date is October 1, 1982.

Conference agreement

The conference agreement follows the House committee provision, effective upon enactment.

14. Technical amendments to social services and foster care

Senate amendment

No provision.

House bill

(1) The 1981 Reconciliation Act (P.L. 97-35) unintentionally repealed the authority for Puerto Rico, Guam, the Virgin Islands, and the Northern Mariana Islands to finance social services from funds received under the cash assistance titles, and provided that these territories are eligible for funds for social services only under the title XX social services block grant.

(2) The formula for allocating funds to the States and territories under the title XX social services block grant program could be interpreted in such a way that a portion of the funds are not available for allocation to any jurisdiction.

(3) There are inconsistencies between titles XI and XX of the Social Security Act as to jurisdictions eligible for title XX funds.

(4) Public Law 97-35 incorrectly referenced child day care instead of foster care standards in the requirements that States have standards for foster family home or child care institutions under their title IV-E foster care program.

The House bill makes the following technical corrections:

(1) Restores the option to Puerto Rico, Guam, the Virgin Islands, and the Northern Mariana Islands to use funds available under the cash assistance titles for social services.

(2) Insures that all the title XX funds under the ceiling are available for allotment to the States and other jurisdictions.

(3) Makes the title XI definition of the term "State," as it pertains to title XX funding, consistent with the list of jurisdictions cited in title XX as eligible for funds under the allotment formula.

(4) Incorporates into the title IV–E foster care law the same standards for foster care as were previously required. (Under prior law these standards were incorporated by reference to the standards in title XX which were in effect prior to Public Law 97–35.) The effective date is October 1, 1981.

Conference agreement

The conference agreement follows the House bill.

SUBTITLE E—CHILD SUPPORT ENFORCEMENT

1. Fee for services to non-AFDC families

Senate amendment

Prior law allowed States to provide child support enforcement services to non-AFDC families without charge or to recover costs of serving such familes by charging the custodial parent an application fee of up to $20, and by retaining a portion of any child support payments which were collected.

An amendment to the 1981 Reconciliation Act replaced this optional provision with a requirement that States impose a fee equal to 10 percent of the support owed, to be charged against the absent parent and added to the amount of the collection.

The Senate amendment repeals the Reconciliation Act amendment and restores the fee provisions of prior law under which States had an option as to whether or not to charge for the costs of non-AFDC child support. It gives States the additional option of allowing them to recover costs either from the absent parent or from the custodial parent.

If a State elects to collect from the custodial parent (by deducting the costs from the amount of child support which is collected) the State must have in effect a procedure under which the court or other entity which determines the amount of the support obligation will be notified of the amount by which any support collection will be reduced to reimburse the costs of collection. The effective date is August 13, 1981.

House bill

The House bill includes the same provision but without the requirement of notification to the court.

Conference agreement

The conference agreement follows the Senate amendment.

2. Allotments from pay for child and spousal support owed by members of the uniformed services on active duty

Senate amendment

The Senate amendment adds a new section to title IV–D of the Social Security Act to require allotments from the pay and allowances of any member of the uniformed service (on active duty) when he fails to make child (or child and spousal) support payments. The requirement would arise when the servicemember failed to make support payments in an amount at least equal to the value of 2 months' worth of support. Provisions of the Consumer Credit Protection Act would apply so that the percentage of the member's pay which could be subject to allotment would be limited. The amount of the allotment would be the amount of the support payment, as established under a legally enforceable administrative or judicial order. The provision is effective October 1, 1982.

House committee provision

The same provision is included. In addition, there is a requirement that the servicemember be given an opportunity (within a 30-day limit) to consult a judge advocate or other law specialist.

Conference agreement

The conference agreement includes the provision in both bills, modified to reflect the House committee provision.

3. Reimbursement of State agency in initial month of ineligibility for AFDC

Senate amendment

Under present law, amounts of child support collected which are sufficient to make the family ineligible for AFDC must be paid to the family beginning with the first month of ineligibility.

The Senate amendment requires that amounts collected which are sufficient to make the family ineligible will be paid to the family in months *after* the first month of ineligibility. This would allow the State to reimburse itself for AFDC that would have already been paid for that month, before the support was collected and known to have made the family ineligible. Thus, the family would not receive double payment for the same month, once in the form of AFDC, and once as a result of the child support collection. The provision is effective October 1, 1982.

House committee provision

The same provision is included, effective upon enactment.

Conference agreement

The conference agreement follows the Senate amendment.

4. Reduction in certain Federal payments to States under the child support enforcement program

Senate amendment

No provision.

House committee provision

The provision reduces the Federal matching rate for State administrative costs from 75 percent to 65 percent, and reduces the child support incentive payments from 15 to 12 percent. In addition, there would no longer be matching for the costs of court personnel who perform child support enforcement functions. The provision is effective October 1, 1982.

Conference agreement

Under the conference agreement, Federal matching for State administrative costs would be reduced from 75 percent to 70 percent, effective October 1, 1982. Child support incentive payments would be reduced from 15 to 12 percent, effective October 1, 1983. Federal matching for the costs of court personnel would be repealed, effective October 1, 1983.

5. Technical amendments to child support enforcement provisions in Reconciliation Act

Senate amendment

No provision.

House bill

The House bill makes several technical corrections in the child support enforcement provisions contained in Public Law 97-35, including inaccurate references. The effective date is October 1, 1981.

Conference agreement

The conference agreement includes the technical corrections.

SUBTITLE F—SUPPLEMENTAL SECURITY INCOME

1. Effective date of application; Proration of initial SSI benefit payment

Senate amendment

SSI benefits in the month of application would be prorated from the date of application or the date of eligibility, whichever is later, instead of the requirement in present law whereby benefits begin the first of the month in which the recipient applies and meets the eligibility requirements. This amendment would also apply to the month in which an individual reapplies after a period of ineligibility. The provision is effective October 1, 1982.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

2. Rounding of SSI eligibility and benefit amounts

Senate amendment

The amendment provides for rounding SSI monthly benefit and income eligibility amounts to the next lower dollar instead of rounding to the next higher ten cents as provided in present law. Rounding would occur after the cost-of-living adjustment had been made. Cost-of-living adjustments in subsequent years would be based on the unrounded benefit and income eligibility amounts so that the provision would have no cumulative effect from year to year. The provision is effective October 1, 1982.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

3. Coordination of SSI and OASDI cost-of-living adjustments

Senate amendment

The Senate amendment continues the provisions in present law whereby SSI benefits are determined on a 2 month retrospective basis, but modifies present law to coordinate SSI and OASDI benefit increases. The amendment provides that at the time the cost-of-living adjustment is made, the recipient's SSI benefit is based on the OASDI benefit received in the same month. Also, whenever the Secretary determines that there is reliable information concerning a recipient's income in a given month, the SSI benefit would be based on that information. The Secretary would be required to prescribe by regulation the circumstances in which such information could be used to determine the monthly SSI benefit. The provision is effective October 1, 1982.

House bill

The House bill repeals retrospective accounting and requires that SSI benefits be determined on the basis of the income anticipated by the recipient in the current month (prospectively). Thus, a social security or other benefit increase expected to be received in a month would be taken into account in determining that month's SSI benefit.

Conference agreement

The conference agreement follows the Senate amendment.

4. Phaseout of hold harmless protection

Senate amendment

The legislation enacting the SSI program included "hold harmless" protection for the States which allowed them to supplement the Federal payment to assure that recipients would receive cash benefits equal to their January 1972 benefit levels, with no cost to the State beyond what was spent for benefits on behalf of aged, blind, and disabled persons in 1972.

Because of Federal benefit increases since that time, all except two States—Hawaii and Wisconsin—have lost their hold harmless status. These two States still receive a Federal contribution to their State supplements because of a special provision added to the law in 1976. Under this provision their hold harmless payments are no longer reduced by Federal benefit increases.

The 1982 Continuing Resolution provided a reduction in hold harmless payments for Wisconsin and Hawaii. The Senate amendment continues phasing out the hold harmless payments. Payments would be reduced to 40 percent of what they would otherwise be in 1983, to 20 percent in 1984, with no "hold harmless" payments made in 1985 and future years. The provision is effective on enactment.

House committee provision

The House committee provision is the same as the Senate amendment but with technical differences.

Conference agreement

The conference agreement follows the House committee provision.

5. Recovery of SSI overpayments

Senate amendment

The Senate amendment would allow the recovery of SSI overpayments from benefits payable under other programs administered by the Social Security Administration (black lung and OASDI benefits.)

House bill.

No provision.

Conference agreement

The conference agreement does not include the Senate amendment.

6. Exclusion from resources of burial plots and certain funds set aside for burial expenses

Senate amendment

The current SSI statute specifies certain assets which an individual may retain without affecting his eligibility for benefits. Excluded are the home, household goods, personal effects, and an automobile of limited value; and liquid assets up to $1,500 in the case of an individual, or $2,250 for a couple.

Also excluded under present law are life insurance policies with cash value, but only if the face value of the policy totals less than $1,500; and burial insurance, irrevocable burial contracts and term life insurance.

The Senate amendment provides that burial spaces for the individual and his immediate family would be excluded as a resource (subject to such limits as to size or value as the Secretary prescribes).

Burial funds for the individual and spouse would also be excluded if they are specifically set aside for this purpose (subject to limits set by the Secretary). Funds set aside that are used for other purposes would reduce future SSI benefits by a like amount. The provision is effective on enactment.

House committee provision

The House committee provision would also exclude burial spaces as a resource as in the Senate amendment but with technical differences. The House committee provision regarding burial funds is the same as the Senate amendment except that it establishes a limit on the amount of funds that can be excluded equal to $1,500 each for the individual and spouse. In addition, funds set aside would reduce on a dollar-for-dollar basis the value of life insurance policies (with cash value) which may be owned by the individual before the cash value is counted. In addition, the $1,500 limit would be reduced by the total of any amounts held by the individual in an irrevocable burial contract or other arrangement made to meet the burial expenses of the individual and spouse. The provision is effective on the first day of the second month after the month of enactment.

Conference agreement

The conference agreement follows the House committee provision but with the following modification:

The Secretary is authorized to exclude as income and resources increases in the value of amounts set aside for burial expenses because of interest earned, and exclude as income and resources any appreciation in the value of specified pre-paid burial arrangements.

7. Mandatory pass-through under State supplementation provisions

Senate amendment

No provision.

House committee provision

The House committee provision modifies present law related to the requirement that States pass through Federal SSI cost-of-living increases. Under present law, a State may meet this requirement by either (1) maintaining the December 1976 level of State supplementation payment for recipients, or (2) providing no less than the total aggregate amount of State supplementation paid by the State in the previous 12-month period. The House committee provision would allow a State to meet the pass-through requirement if the State did not decrease the State supplementation payment below the level in the previous December instead of the December 1976 level required under present law. The provision would be effective for 12-month periods ending after June 1982.

Conference agreement

The conference agreement follows the House committee provision.

8. Treatment of unnegotiated checks under the supplemental security income program

Senate amendment

No provision.

House bill

Under present law, States are credited with their share (included as State supplementation) of benefit checks remaining unnegotiated for more than 180 days. The House bill clarifies the authority for the Federal Government to credit States for unnegotiated SSI benefit checks which are "State supplementation only" checks. The provision is effective October 1, 1982.

Conference agreement

The conference agreement follows the House bill.

SUBTITLE G—UNEMPLOYMENT COMPENSATION

1. Rounding of unemployment benefits to next lowest dollar

Under present law, States may determine rounding procedures to apply in the calculation of an individual's weekly unemployment benefit. Regular benefits are financed solely by State trust funds. Extended benefits are financed 50 percent from State trust funds and 50 percent from Federal unemployment insurance trust funds.

Senate amendment

The Federal 50 percent matching share of extended unemployment benefits would not be available on that part of extended unemployment benefit payments which result from a failure on the part of the State to have a benefit structure in which benefits are rounded down to the next lower dollar. This provision is effective for benefits payable on or after October 1, 1983. States in which there is no legislative session prior to that date would, however, be given additional time before the provision would become effective.

House bill

No provision.

Conference agreement

The conference agreement follows the Senate amendment.

2. Use of amounts transferred to State unemployment funds pursuant to the Reed Act

Section 903 of the Social Security Act, commonly referred to as the Reed Act, provides for the transfer of any excess Federal Unemployment Tax Act (FUTA) receipts to the individual State accounts in the unemployment Trust Fund. Each State's share is proportionate to its share of wages subject to FUTA taxes. Excess funds have occurred only three times since the passage of the Reed Act—in 1956, 1957, and 1958. Current unobligated balances in the State Reed Act accounts total $25 million.

Reed Act funds may be used by the States either to pay unemployment benefits or for administrative purposes. However, under present law, authority to use funds credited in 1956 and 1957 for administrative purposes has expired; and authority to use funds credited in 1958 for administrative purposes will expire on July 1, 1983.

Senate amendment

No provision.

House bill

The House provision extends for 10 years the authority for States to use Reed Act funds for administrative purposes. Also, the provision permits States that have used such funds to pay unemployment benefits to reestablish a Reed Act account based on the amount of funds previously distributed to those States under the Reed Act. The provision is effective the date of enactment.

Conference agreement

The conference agreement follows the House bill.

3. Unemployment benefits paid to ex-servicemembers

Under the program for unemployment compensation payments to ex-servicemembers (UCX), benefits are limited to individuals who (1) have 365 or more days of military service; (2) were discharged or released under honorable conditions; (3) did not resign or voluntarily leave the service (i.e., they could not have been able to reenlist); and (4) were not released or discharged "for cause" as defined by the Department of Defense. These requirements apply to individuals who left Federal military service on or after July 1, 1981, but only for weeks of unemployment that began on or after August 19, 1981.

Senate amendment

No provision.

House bill

The House provision substitutes new unemployment compensation eligibility requirements for individuals separated from the military. The provision (1) limits unemployment benefits to ex-servicemembers who have served 730 or more continuous days in the military and who have been discharged under other than dishonorable conditions; (2) requires a 4-week waiting period between the week in which the individual separated and the week in which he or she first becomes entitled to compensation; and (3) limits an eligible ex-servicemember's benefit to 13 weeks. The provision is effective for those separated from the service on or after July 1, 1981, but only for benefits payable after the date of enactment.

Conference agreement

The conference agreement does not include the House provision.

4. Additional weeks of unemployment compensation benefits: Federal supplemental benefits (Title 6 of Conference Report)

Most States provide up to a maximum of 26 weeks of State unemployment compensation benefits to unemployed individuals who meet the qualifying requirements of State law. Many claimants qualify for less than the maximum 26 weeks of State benefits. State benefits are financed out of State unemployment trust funds.

Under the permanent Federal-State extended benefits program, additional weeks of unemployment compensation are payable to individuals who exhaust their State benefits during periods of high unemployment. No one may receive more than 13 weeks of extended benefits, or more than 39 weeks of State plus extended benefits. Extended benefits are financed one-half out of State unemployment trust funds and one-half out of Federal unemployment trust funds.

Until September 25, 1982, extended benefits are payable in a State when, for the most recent 13-week period, the State insured unemployment rate (IUR)[1] averages at least 5 percent and, in addition, is 20 percent higher than it was during the same 13-week period in the 2 previous years. When the "20 percent" factor is not met, a State, at its option, may provide extended benefits when the State IUR averages 5 percent. (Thirty-nine States have incorporated the optional 5-percent trigger into their State law.)

Effective September 25, 1982, the IUR at which extended benefits will be payable in any State will be raised from 4 percent (plus the 20-percent factor) to 5 percent (plus the 20-percent factor). The optional trigger rate will be increased from 5 percent to 6 percent. (This change was made by the 1981 Budget Reconciliation Act.)

Senate amendment

No provision.

House committee provision

An individual who exhausts State and extended benefits could receive additional weeks of benefits, Federal supplemental benefits (FSB), equal to one-half of the duration of the claimant's State benefit entitlement. No one could receive more than 13 additional weeks or a combined maximum of more than 52 weeks of State benefits plus extended benefits plus the additional weeks provided by this provision. Benefit and administrative costs of the additional weeks would be financed out of general revenue.

The additional weeks of benefits (FSB) would be payable under the same triggers used to trigger on the extended benefits program. In other words, FSB would be payable wherever extended benefits were payable. FSB would be payable from date of enactment through September 30, 1983.

Conference agreement

The conference agreement provides, effective September 12, 1982 through March 31, 1983, up to 10 additional weeks of unemployment compensation benefits for unemployed workers in States in which extended benefits are being paid or have been paid at any time since June 1, 1982. Up to 8 additional weeks of benefits would be provided in States in which the extended benefit trigger rate equals or exceeds 3.5 percent. Up to 6 additional weeks of unemployment benefits would be provided in all other States.

If at any time 10 additional weeks of benefits are or become payable in a State, qualified unemployed workers in the State will be able to receive up to 10 weeks of benefits throughout the duration of the program, regardless of changes in the extended benefit trigger rates in the State.

The additional weeks of benefits would be paid to unemployed workers whose entitlement to State benefits (i.e., benefit year) or extended benefits ended on or after June 1, 1982; and

(a) who have no rights to regular or other State benefits or Federal/State extended benefits;

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[1] The insured unemployment rate (IUR) is the percentage of workers covered by the State unemployment compensation program who are claiming State benefits.

(b) who have worked 20 or more weeks or have the equivalent in wages (i.e., 40 times the weekly benefit amount or one and one-half times high quarter wages, as specified in the extended benefits program) during the State defined base-period (generally a 12 month period prior to the time the person filed for State unemployment compensation); and,

(c) who continue to meet all other State and extended benefit requirements.

Except in States in which 10 additional weeks are or became payable, an individual's eligibility would be determined on a week by week basis according to the situation prevailing in the State. For example, an individual who initially qualifies for 6 weeks of benefits under this program (because the State extended benefit trigger rate is under 3.5 percent) may receive an additional 2 or 4 weeks of benefits if the rate subsequently increases (even if this occurs some weeks after he exhausts his 6-week entitlement). Similarly an individual who draws his first week of benefits under this program at a time when the State meets the 8-week criteria will not be eligible for a seventh or eighth week of benefits if the State extended benefit trigger rate drops below 3.5 percent before he receives the seventh and eighth week of benefits.

The determination of whether a State has a rate of 3.5 percent or more will be determined in the same manner as the extended benefit triggers: that is, on the basis of the average of the rates prevailing during a 13-week period ending 3 weeks previously. The determination for the week of September 12, 1982, the first week this program is in effect, will be based on the 13-week period ending August 28, 1982.

5. Taxation of unemployment compensation (Title 6 of Conference Report)

Under present law, the amount of State and Federal unemployment insurance benefits included in adjusted gross income for income tax purposes is equal to the lower of:

(a) the amount of unemployment benefits paid, or

(b) one-half of the excess of adjusted gross income, unemployment benefits, and excludable disability income over $20,000 for single taxpayers, $25,000 for married taxpayers filing jointly, or zero for married taxpayers filing separately.

Senate amendment

No provision.

House committee provision

The income thresholds limiting inclusion of unemployment benefits in adjusted gross income would be reduced to $12,000 for single taxpayers and $18,000 for married taxpayers filing jointly. Penalties for underpayment of estimated tax for 1982 attributed to this change would be waived. The provision is effective for benefits paid on or after January 1, 1982.

Conference agreement

The conference agreement follows the House committee provision.

6. Interest on State unemployment loans transferred to Extended Unemployment Compensation Account (EUCA).

Under current law, States must pay interest on unemployment loans (as described in item 12). The interest payments are credited to the General Fund of the U.S. Treasury.

Senate amendment

No provision.

House committee provision

The House committee provision provides that interest paid by the States on Federal unemployment loans after December 31, 1982, would be credited to the Extended Unemployment Compensation Account (EUCA), one of three accounts in the Federal Unemployment Trust fund. EUCA finances the 50 percent Federal share of the Federal-State extended benefits program.

Conference agreement

The conference agreement does not include the House provision.

7. Treatment of certain employees of institutions of higher education

Under present law, employees of institutions of higher education and employees of elementary and secondary schools are covered by the unemployment insurance system. However, Federal law requires States to deny benefits during school recess periods to those individuals employed in an instructional, research, or principal administrative capacity under certain conditions. Benefits are denied for any week commencing during the period between two successive academic years or terms if an employee worked during the first term and has a contract or reasonable assurance of reemployment in the second year or term. This between-term denial may also be extended, at State option, to nonteaching, nonresearch, and nonprincipal administrative employees of elementary and secondary schools, but not to similar employees of colleges and universities.

Senate amendment

No provision.

House committee provision

Upon enactment, the House committee provision would allow States to deny unemployment compensation benefits to nonteaching, nonresearch, and nonadministrative employees of colleges and universities during periods between academic years or terms, if there is reasonable assurance the individual will be employed by the institution at the beginning of the forthcoming academic year or term. This would make Federal law consistent in its policy toward such employees of all educational institutions. The House committee provision also provides that retroactive benefits may be received by certain nonteaching, nonresearch, and nonadministrative educational employees who were reasonably assured of employment in the second term or in the fall, but were subsequently not offered that employment. Such retroactive benefits could be provided only for weeks during the between-term or recess period for which the person filed a timely claim for benefits and, except for the denial authority provided under this section, would have been eligible to receive benefits.

Conference agreement

The conference agreement follows the House committee provision.

8. Short-time compensation

Under current law, all States provide partial unemployment benefits for claimants who work less than regular full-time hours (as defined by State law). However, most State unemployment insurance laws do not allow partial benefits in a way that encourages "worksharing" and short-time compensation (partial, prorated unemployment benefits to workers whose work-week is reduced in lieu of total layoff of some of a firm's employees). This is because partial benefits under present law generally end when a worker earns slightly more than one-half of full-time wages.

Senate amendment

No provision.

House committee provision

The House committee provision directs the Department of Labor (DOL), upon enactment, to develop model legislation that can be used by States wishing to establish short-time compensation (or "worksharing") programs. DOL is directed to evaluate the operation and impact of any such programs implemented by the States and report its findings to Congress no later than October 1, 1985.

Conference agreement

The conference agreement follows the House committee provision.

TABLE 1.—RECONCILIATION INSTRUCTION

[In millions of dollars]

	Fiscal Year—			Total
	1983	1984	1985	
Senate Finance	4,429	5,564	5,976	15,969
Ways and Means	3,755	4,827	5,168	13,750
Medicare [1]	3,162	4,122	4,240	11,524
Medicaid [1]	674	737	808	2,219
Public Assistance [1]	593	705	928	2,226

[1] The committees are reconciled only to the total outlay savings. The figures shown for each program represent assumptions used in arriving at the total reconciliation instructions, and are not binding.

TABLE 2.—CONFERENCE AGREEMENT[1] (PRELIMINARY ESTIMATES)

[In millions of dollars]

	Fiscal Year—			Total
	1983	1984	1985	
Total savings	3,695	5,896	7,865	17,456
Medicare	2,879	4,430	5,998	13,307
Medicaid	275	364	502	1,141
Aid to families with dependent children (AFDC)	85	95	163	343
Child support enforcement (CSE)	92	141	151	384
Supplemental security income (SSI)	116	126	144	386
Unemployment compensation (UC)	−81	49	49	17
Debt management	329	691	858	1,878

[1] This table does not reflect the additional food stamp outlays of $184 million, and additional medicaid outlays of $111 million resulting from two medicare provisions over the three-year period. Thus the total net outlays savings are $17,161 million. The table reflects the savings to each of the programs identified. The minus sign (−) for 1983 in unemployment compensation represents additional outlays.

TABLE 3.—BUDGET IMPACT OF EACH PROVISION WITHIN THE CONFERENCE AGREEMENT

[− means increase in outlays; figures in millions]

	Fiscal year—			Total
	1983	1984	1985	
MEDICARE				
2. Medicare secondary for older workers	$350	$530	$600	$1,480
4. 80 percent radiologist/pathologist (medicaid cost of $50 million)	160	210	250	620
7. Elimination of nursing differential	95	110	125	330
8. Hospital-based physicians	63	73	84	220
9. Part B premium as a constant percentage of costs (medicaid cost of $61 million)	45	240	480	765
10. Compromise—hospital reimbursement (medicaid savings of $280 million)	480	1,770	3,770	6,020
11. Elimination of private room subsidy	54	75	80	209
12–13. Single reimbursement limit for skilled nursing facilities and home health agencies	18	46	46	110
14. Elimination of duplicate payments for outpatient services	160	225	270	655
15. Audit and medical claims review	130	300	300	730
16. Temporary delay in periodic interim payments	750	100	−870	−20
17. Reimbursement of assistants at surgery	55	130	150	335
19. Prohibition of payments for ineffective drugs	0	0	0	0
20. Medicare payments to HMO's	0	0	0	0
21. Technical corrections	0	0	0	0
22. Hospice care	−3	−1	17	13
23. Coverage of extended care services	0	0	0	0
24. Percentage arrangements (not for hospital-based physicians)	15	17	20	52
25. Interest on overpayments	25	25	20	70
26. Prohibit payment for Hill-Burton care	15	17	20	52
27. Prohibiting payment for antiunionization activities	0	0	0	0
28. Lesser of cost or charges	$0	$0	$0	$0
29. Extend medicare proficiency exam	0	0	0	0
30. Access to books and records	0	0	0	0
31. Private sector utilization review	330	385	440	1,155
32. Part B enrollment	(3)	(3)	(3)	(3)
Subtitle C—Utilization and quality control peer review	15	15	20	50
HI tax for Federal employees (outlay savings)	122	163	176	461
Total medicare provisions	2,879	4,430	5,998	13,307
MEDICAID				
1. Copayments by medicaid recipients	45	50	56	151
3. Modification in lien provisions	165	180	200	545
4. Error rate sanctions	30	65	72	167
6. Coverage of disabled children at home	(3)	(3)	(3)	(3)
7. Technical corrections	0	0	0	0

TABLE 3.—BUDGET IMPACT OF EACH PROVISION WITHIN THE CONFERENCE AGREEMENT—Continued

[— means increase in outlays; figures in millions]

	Fiscal year—			Total
	1983	1984	1985	
8. American Samoa	−1	−1	−1	−3
9. Nursing home moratorium	0	0	0	0
Hospital reimbursement	20	80	180	280
AFDC impact on medicaid	16	20	25	61
Offset to last year's penalty	0	−30	−30	−60
Total medicaid provisions	275	364	502	1,141
Impact on medicaid of:				
80 percent radiologist/pathologist [1]	−15	−15	−20	−50
Part B premium [1]	−4	−19	−38	−61
AFDC				
1. Round AFDC benefits	9	10	10	29
2. Prorate AFDC benefits	13	14	14	41
3. Military service/AFDC	15	17	17	49
5. Optional job search	5	10	15	30
8. Prorate shelter and utilities	43	44	45	132
9. Error rate sanctions	0	0	62	62
11. Exclusion from AFDC income of certain state payments	0	0	0	0
12. Extend WIN demonstration	0	0	0	0
13. Exclude State payments to children	0	0	0	0
14. Technical amendments	0	0	0	0
Total AFDC provisions	85	95	163	343
Food stamp impact of AFDC provisions [2]	−39	−44	−46	−129
CSE				
1. Non-AFDC fees	12	16	11	39
2. Military allotments	7	9	10	26
3. Initial month of ineligibility	3	4	4	11
4. Reduce Federal CSE incentive funds and administrative costs	70	112	126	308
5. Technical amendments	0	0	0	0
Total CSE provisions	92	141	151	384
SSI				
1. Prorate SSI benefits	26	28	32	86
2. Round SSI benefits	20	25	30	75
3. SSI accounting period	45	41	43	129
4. Phase out hold harmless	30	37	45	112
6. Exclude burial plots and contracts	−5	−5	−5	−15
7. Mandatory passthrough under SSI	0	0	0	0
8. Unnegotiated SSI checks	0	0	−1	−1
Total SSI provisions	116	126	144	386
Food stamp impact of SSI provisions [2]	−17	−18	−20	−55
UC				
1. Rounding UC benefits	0	10	19	29
2. Extend Reed Act	0	0	0	0
7. Treatment of school employees	7	8	9	24
8. Short time compensation	−1	−1	0	−2
Deferral of interest payment on UC loans	−87	32	21	−34
Total UC provisions	−81	49	49	17

Footnotes at end of table.

TABLE 3.—BUDGET IMPACT OF EACH PROVISION WITHIN THE CONFERENCE AGREEMENT—Continued

[– means increase in outlays; figures in millions]

	Fiscal year—			Total
	1983	1984	1985	
DEBT MANAGEMENT				
1. Savings bonds	329	691	858	1,878

[1] Increased medicaid outlays due to changes in medicare are scored against total savings for the House, but not the Senate.

[2] Increased food stamp outlays are scored against total savings for the House, but not the Senate.

[3] Negligible cost.

Note: The estimates for each provision of outlay savings within each program (e.g. Medicare) reflect the savings to that program and not necessarily the total budget impact. If a provision has an impact upon two programs, it is listed twice.

In addition, there is a loss in revenue from item 2 under Medicare (Medicare secondary for older workers) of $85,130 million and 150 million for fiscal years 1983 to 1985 respectively.

TABLE 4.—Budget Impact of the Provisions to Lower Unemployment Compensation Tax Thresholds and to Provide Federal Supplemental Benefits

(– indicates an expenditure reduction or revenue increase; + indicates an expenditure increase; figures in millions)

	Fiscal year—				Total
	1982	1983	1984	1985	
Lower unemployment compensation tax thresholds (additional revenues)	0	–763	–734	–611	–2,108
Federal supplemental benefits (additional outlays)	175	1,919	0	0	2,094
Administrative cost (additional outlays)	0	20	0	0	20
Impact on food stamps and AFDC (reduced outlays)	0	–209	0	0	–209
Total impact on budget deficit [1]	+175	+967	–734	–611	–203

[1] + means an increase in the deficit; – means a decrease in the deficit.

PART TWO

REVENUE PROVISIONS

CONTENTS OF REVENUE PROVISIONS

Page

Titles II, III and IV—Revenue Provisions 473
- A. Individual Income Tax Provisions 473
  - 1. Individual minimum tax 473
  - 2. Deduction for medical expenses 476
  - 3. Deduction for casualty losses 476
  - 4. Capital gains holding period 477
  - 5. Capital gains indexing 478
- B. Business Tax Provisions 478
  - 1. Corporate tax preferences 478
  - 2. Basis adjustment for investment tax credits 481
  - 3. Limitation on investment tax credit 482
  - 4. Accelerated depreciation (ACRS)—1985 and 1986 483
  - 5. Construction period interest and taxes 484
  - 6. Leasing rules 487
    - a. Non-safe harbor leasing rules 487
    - b. Safe harbor leasing rules 492
  - 7. Foreign provisions 501
    - a. Limitations on amount of foreign oil and gas extraction taxes allowed as foreign tax credits 501
    - b. Current taxation of foreign oil and gas non-extraction income 502
    - c. Possessions and Virgin Islands corporations 504
  - 8. Tax-exempt obligations 514
    - a. Restrictions on tax-exempt bonds for private activities 514
    - b. Other amendments affecting industrial development bonds 521
    - c. Mortgage subsidy bonds 525
  - 9. Mergers and acquisitions 528
    - a. Partial liquidations 528
    - b. Certain distributions of appreciated property 532
    - c. Stock purchases treated as asset purchases 535
    - d. Reorganizations constituting changes in form 540

CONTENTS OF REVENUE PROVISIONS—Continued

Page

e. Use of holding companies to bail out earnings 541
f. Application of attribution rules 544
g. Waiver of family attribution rules 544
10. Accounting for long-term contracts 547
11. Accelerated corporate tax payments 551
12. Amortization of original issue discount 553
13. Tax treatment of stripped bonds 554
14. Business meals and tip income 556
15. ITC for soil or water conservation expenditures 559
16. Public utility dividend reinvestment plans 559
C. COMPLIANCE PROVISIONS 560
1. Withholding on interest and dividends 560
2. Other compliance provisions 562
a. Reporting of interest 562
b. Obligations required to be registered 563
c. Returns of brokers 565
d. Information reporting requirements for payments of remuneration for services and direct sales 565
e. Reporting of State and local income tax refunds 567
f. Increased penalties for failure to file information returns and statements 568
g. Increase in civil penalty on failure to supply identifying numbers 569
h. Extension of withholding to certain payments where identifying number not furnished or inaccurate 569
i. Minimum penalty for extended failure to file 571
j. Forms of returns 571
k. Penalty for promoting abusive tax shelters, etc 572
l. Action to enjoin promoters of abusive tax shelters, etc 573
m. Procedural rules applicable to penalties under sections 6700, 6701, and 6702 573
n. Penalty for substantial understatement 574
o. Penalty for aiding and abetting the understatement of tax liability 576
p. Fraud penalty 577
q. Frivolous returns 578
r. Criminal fines 578
s. Adjustments to estimated tax provision 579
t. Special rules with respect to certain cash 580
u. Special procedures for third-party summonses and third-party recordkeepers 583

CONTENTS OF REVENUE PROVISIONS—Continued

Page
- v. Limitation on use of administrative summonses 584
- w. Withholding on pensions, annuities, and certain deferred income 584
- x. Pension reporting requirement 586
- y. Pension recordkeeping requirements 587
- z. Partial rollovers of IRAs 587
- aa. Foreign investment in U.S. real property ... 588
- bb. Returns with respect to foreign personal holding companies 588
- cc. Penalty for failure to furnish information returns with respect to certain foreign corporations; reporting requirement for corporations controlled by foreign persons 589
- dd. Access to records and persons not found in the United States 590
- ee. Authority to delay date for filing certain returns relating to foreign corporations and trusts 594
- ff. Technical amendment to section 905(c) 595
- gg. Daily compounding of interest 595
- hh. Semi-annual determination of rate of interest 596
- ii. Restrictions on payment of interest for certain periods 596
- jj. Disallowing deductions for drug dealing 597
- kk. Internal Revenue Service staff increases 598
- ll. Reports on forms 598

3. TAX TREATMENT OF PARTNERSHIP ITEMS 599
- a. In general 600
- b. Administrative proceedings 600
- c. Judicial review of FPAA 603
- d. Request for administrative adjustment 604
- e. Statute of limitations on assessments 606
- f. Computational adjustments 607
- g. Limitations applicable to credits and refunds 607
- h. Certain other rules 608
- i. Small partnerships 608
- j. Certain definitional and other rules 609
- k. Nonpartnership litigation 610
- l. Foreign-based partnerships 611
- m. Partnership must provide information to partners 612
- n. Effective date 612
- o. Windfall profit tax audits 612

4. TAXPAYER SAFEGUARD PROVISIONS 614
- a. Property exempt from levy 615
- b. Release of lien 615
- c. Notice before levy 615

CONTENTS OF REVENUE PROVISIONS—Continued

Page

d. Redemption of property 616
e. Amount of damages in case of wrongful levy 616
f. Notice of procedural safeguards 616

D. PENSION PROVISIONS 617
1. Overall limits on contributions and benefits 617
2. Loans from retirement plans 618
3. Parity between corporate and noncorporate plans; group-term life insurance 620
4. Retirement savings for church employees 636
5. State judicial retirement plans 639
6. Profit-sharing, etc., contributions for disabled employees 639
7. Participation in group trusts by governmental plans 640

E. INSURANCE PROVISIONS 641
1. Reinsurance arrangements 641
2. Policyholder dividends 642
3. Life insurance reserves and contract liabilities 643
4. Menge formula 644
5. Consolidated returns 645
6. Allowance of deduction for excess interest 646
7. Amounts received under annuity contracts 646
8. Flexible premium contracts 647
9. Indeterminate premium policies 649
10. Underpayment of 1982 estimate taxes 649

F. EMPLOYMENT TAX PROVISIONS 650
1. Independent contractors 650
a. Alternative standards for determining classification of workers for employment tax purposes and extension of interim relief provision 650
b. Reduction of certain employment tax liabilities where workers are reclassified as employees 651
c. Tax Court jurisdiction over certain employment tax issues 652
2. Federal unemployment tax (FUTA) provisions 653
a. FUTA tax rate 653
b. Exclusion from FUTA of wages paid to certain students 656
c. Extension of exclusion from FUTA of wages paid to certain alien farmworkers 656
3. Extension of social security hospital insurance taxes and Medicare coverage to Federal employees 657

G. EXCISE TAX PROVISIONS 659
1. Airport and airway taxes 659
2. Increase in cigarette excise taxes 662
3. Increase in telephone excise tax 663

CONTENTS OF REVENUE PROVISIONS—Continued

Page

- 4. Windfall profit tax provisions 663
  - a. Windfall profit tax TAPS adjustment repeal 663
  - b. Windfall profit tax on Alaska Native Corporations 664
- 5. Expansion of Dingell-Johnson Fund taxes 664

H. OTHER PROVISIONS 666

- 1. Exclusion from income of National Research Service Awards 666
- 2. Annual accrual accounting method for certain joint ventures 666
- 3. Extension and revision of targeted jobs credit 667
- 4. Certain payments to foreign government officials or employees 669
- 5. Debt management provisions 670
  - a. Rate of interest on U.S. savings bonds 670
  - b. Long-term U.S. bonds 670
- 6. Disclosure of tax returns 671
  - a. Disclosure of tax return information for nontax criminal investigation purposes 671
  - b. Civil damages for unauthorized disclosure of returns and return information 676
  - c. Disclosure of returns and return information for use in certain audits by the General Accounting Office 676
- 7. Veterans organizations 679
- 8. Amateur athletic organizations 679
- 9. Applicability of private foundation rules 680
- 10. Clarification of tax status of certain members of religious orders 682
- 11. Study of alternative tax systems 682
- 12. Study of monetary policy 684
- 13. New Jersey general revenue sharing allocation 684
- 14. Relief for the Jefferson County Mental Health Center, Lakewood, Colo 684
- 15. Award of reasonable litigation costs where taxpayer prevails and government position was unreasonable 686
- 16. Personal holding companies 687
- 17. Additional refunds relating to repeal of the excise tax on buses 688
- 18. Modification of rules as to acceleration of accrual of taxes 688
- 19. Reassigning VHF television licenses 690

Revenue Effects of Tax Provisions of H.R. 4961 as Agreed to by the Conference Committee 691

CONTENTS OF REVENUE PROVISIONS—Continued

Page

TABLE 1. SUMMARY OF ESTIMATED REVENUE EFFECTS OF TAX PROVISIONS OF H.R. 4961 AS AGREED TO BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1983-1987 691

TABLE 2. ESTIMATED REVENUE EFFECTS OF TAX PROVISIONS OF H.R. 4961 AS AGREED TO BY THE CONFERENCE COMMITTEE, FISCAL YEARS 1983-1987 693

TITLES II, III AND IV—REVENUE PROVISIONS

A. Individual Income Tax Provisions

1. Individual minimum tax

Present law

A 15-percent add-on minimum tax is imposed on the sum of six tax preferences in excess of the greater of one-half the regular income tax paid or $10,000. The tax preference items included in the minimum tax base are:

(1) Accelerated depreciation on real property in excess of straight-line depreciation over the useful life or recovery period;

(2) Accelerated depreciation on personal property subject to a lease;

(3) Amortization of certified pollution control facilities (the excess of 60-month amortization over depreciation otherwise allowable);

(4) Percentage depletion in excess of the adjusted basis of the property;

(5) Amortization of child care facilities (the excess of 60-month amortization over depreciation otherwise allowable);

(6) Intangible drilling costs on oil, gas and geothermal wells in excess of the amount amortizable with respect to these costs, and in excess of net income from production.

Individuals are also subject to an alternative minimum tax, payable to the extent it exceeds regular tax. The base of this tax is taxable income increased by:

(1) the deduction for long-term capital gains, and

(2) itemized deductions (other than for medical expenses, casualty losses and taxes) to the extent that the total amount exceeds 60 percent of adjusted gross income reduced by these 3 excluded deductions.

The alternative minimum tax base is subject to the following rates:

	Percent
$0 to $20,000	0
$20,000 to $60,000	10
Over $60,000	20

For estates, trusts, and married individuals filing separate returns the dollar amounts defining the tax brackets are one-half the above amounts. The foreign tax credit is allowed, and credits attributable to an active trade or business are allowed to the extent that tax is not attributable to net capital gains or to itemized deductions included in the minimum tax base.

For purposes of both the regular and minimum taxes, individuals may elect to expense all intangible drilling costs for oil, gas and geothermal properties. The amount expensed in excess of the amount which would be allowed if these costs were amortized, and in excess of net income from production, is an item of tax preference (item (6), above).

House bill

No provision.

Senate amendment

The add-on minimum tax is repealed for individuals.

The base of the alternative minimum tax is changed to be equal to adjusted gross income plus specified preferences, minus specified itemized deducations.

The specified preferences include:

(1) the 6 preferences presently included under the add-on minimum tax;

(2) the deduction for long-term capital gains;

(3) interest and dividend income excluded under the $100 dividend exclusion, the All-Savers exclusion, and the 15-percent net interest exclusion (which takes effect after 1984); and

(4) the excess of expensing over 120-month amortization for mining exploration and development costs, research and development costs, and magazine circulation expenditures.

Deductions are allowed for the following to the extent not deductible in arriving at adjusted gross income:

(1) charitable contributions;

(2) medical expenses (in excess of 10 percent of adjusted gross income);

(3) casualty losses (in excess of 10 percent of adjusted gross income);

(4) personal housing interest;

(5) other interest to the extent of net investment income; and

(6) estate taxes.

The net operating loss deduction is generally reduced by items of tax preference.

The rates of the alternative minimum tax are changed as follows:

Unmarried individuals	*Percent*
$0 to $30,000	0
$30,000 to $50,000	10
Over $50,000	20

Married couples filing joint returns and surviving spouses	*Percent*
$0 to $40,000	0
$40,000 to $60,000	10
Over $60,000	20

For estates, trusts, and married individuals filing separate returns, the dollar amounts defining the tax brackets are one-half the amounts applicable to married couples filing joint returns. The foreign tax credit is allowed. Other non-refundable credits are not allowed.

Individuals may elect to capitalize a portion of their intangible drilling costs, except with respect to interests in which they are limited partners. These capitalized costs are treated as 5-year ACRS property, and allowed a 10-percent investment credit. Taxpayers must reduce the ACRS deductions to take account of the half-basis adjustment. These costs are not eligible for safe-harbor leasing. The ACRS deductions are not treated as an item of tax preference.

The Senate amendment generally applies to taxable years beginning after December 31, 1982. Pre-1983 net operating loss preferences continue to be subject to the add-on tax when used, as under present law.

Conference agreement

The conference agreement generally follows the Senate amendment. The tax rate is revised so that the entire minimum taxable income in excess of the exemption amount is taxed at a 20-percent rate. In addition, the minimum tax preference for amortization of child care facilities is deleted, and a preference is added for the excess of the fair market value of stock received upon the exercise of an incentive stock option over the exercise price. It is intended that the incentive stock option preference not apply where there is an early disposition of the stock acquired through the exercise of the option. Wagering losses allowable under section 165 will be allowable as a deduction in computing the minimum tax base.

An election is provided for individuals to amortize the mining exploration and development costs, circulation expenditures, and research and experimental expenditures, for purposes of the regular tax and minimum tax, over a 10-year period beginning with the year the expenditure occurs. The preference item with respect to these costs is revised to equal the excess of expensing over 10-year, rather than 120-month amortization. Individuals thus will not have a preference from these costs to the extent that they elect 10-year amortization. With respect to intangible drilling costs, limited partners may elect 10-year amortization. For other individuals with intangible drilling costs, the conference agreement provides the same election to use ACRS treatment and the investment tax credit that is provided by the Senate amendment.

Finally, the agreement provides that net income taken into account, directly or indirectly, from a limited partnership interest or an interest in a subchapter S corporation (in the case of a person who does not participate in the management of the corporation) will be investment income for the purposes of the net investment income limitation on the interest deduction. Further, interest on indebtedness incurred to acquire or carry such an interest will be "below the line" interest for purposes of the minimum tax and therefore subject to the net investment income limitation on the interest deduction. No inference is intended as to the proper treatment under the regular tax.

2. Deduction for medical expenses

Present law

Individuals who itemize deductions may deduct two categories of medical expenses:

(1) up to $150 for one-half of health insurance premiums.

(2) all other unreimbursed medical expenditures, including health insurance premiums not allowed in the first category, to the extent that these expenses exceed 3 percent of adjusted gross income. Drug expenditures may be included only to the extent the total of drug expenditures exceeds 1 percent of adjusted gross income.

House bill

No provision.

Senate amendment

The medical expense deduction is modified as follows:

(1) the $150 ceiling on the deduction for one-half of health insurance premiums is reduced to $100.

(2) the floor for deductible medical expenses is raised from 3 percent to 7 percent of adjusted gross income.

The provision is effective for taxable years beginning after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment, with several modifications. First, the separate $150 deduction for one-half of health insurance premiums is eliminated. Second, the floor for deductible medical expenses is raised from 3 percent to 5 percent of adjusted gross income. These first two provisions are effective for taxable years beginning after December 31, 1982. Third, effective for taxable years beginning after December 31, 1983, the one-percent floor under drug expenditures is eliminated, and the only drug expenditures which will be deductible will be expenditures for drugs which legally require a prescription or for insulin.

3. Deduction for casualty losses

Present law

Individuals who itemize deductions may deduct unreimbursed losses of nonbusiness property resulting from fire, storm, shipwreck, or other casualty, or from theft. The amount of the loss is the lower of (1) the fair market value of the property immediately before the casualty, reduced by the fair market value of the property immediately after the casualty (zero in the case of a theft) or (2) the property's adjusted basis. For any one casualty, the deduction is allowed only to the extent that the amount of the loss exceeds $100.

House bill

No provision.

Senate amendment

Effective for taxable years beginning after December 31, 1982, nonbusiness casualty losses are deductible only to the extent total losses sustained during the year exceed 10 percent of adjusted gross income. As under present law, each casualty loss will be deductible only to the extent it exceeds $100.

Conference agreement

The conference agreement follows the Senate amendment, with a technical amendment. The amendment makes clear that individuals who elect to take into account a nonbusiness disaster loss for the taxable year prior to the taxable year in which the disaster occurred must use the adjusted gross income of the prior taxable year in determining the extent to which the loss is deductible.

Although the amendments made by the conference agreement generally apply to taxable years beginning after December 31, 1982, the amendments also apply to the taxpayer's last taxable year beginning before January 1, 1983, for a taxpayer who elects to take into account a disaster loss in such a taxable year. For example, if a calendar year taxpayer experiences a disaster loss in 1983 and elects to claim the loss for calendar year 1982, the loss will be deductible only to the extent it exceeds 10 percent of the taxpayer's 1982 adjusted gross income.

4. Capital gains holding period

Present law

Gains or losses on certain assets held more than 12 months are considered long-term capital gains.

For noncorporate taxpayers, 40 percent of net long-term capital gains are included in income, while 100 percent of net short-term gains are included. However, 100 percent of net short-term losses (up to $3,000) are deductible, while only 50 percent of net long-term losses (up to $3,000) are deductible.

For corporate taxpayers, net long-term gains are subject to an alternate tax rate of 28 percent, while net short-term gains are taxed at ordinary corporate rates.

House bill

No provision.

Senate amendment

The holding period distinguishing long-term from short-term capital gains and losses is reduced to 6 months, effective for assets sold or exchanged after June 30, 1982.

Conference agreement

The conference agreement does not include the Senate amendment.

5. Capital gains indexing

Present law

The adjusted basis for determining the gain or loss from the sale or other disposition of property is established in fixed dollar amounts and, thus, does not take into account changes in the value of the dollar resulting from inflation.

House bill

No provision.

Senate amendment

The basis of certain assets is adjusted for inflation in order to determine the gain or loss upon the sale or other disposition of the assets.

Assets eligible for the indexing adjustments are corporate stock and real property that are capital assets or assets used in a trade or business and are held for more than one year.

The inflation adjustment is based on the level of the GNP deflator for the quarter the asset is purchased compared with the deflator for the quarter of sale. However, if the asset was purchased before 1985, the base is the GNP deflator in the fourth quarter of 1984.

Special rules are provided for certain conduit entities to ensure that an appropriate portion of the inflation adjustments flow through to shareholders or partners.

The provision applies to sales and exchanges after December 31, 1984.

Conference agreement

The conference agreement does not include the Senate amendment.

B. Business Income Tax Provisions

1. Corporate minimum tax

Present law

Corporations must pay a minimum tax on certain tax preferences. The tax is in addition to the corporation's regular tax. The amount of the minimum tax is 15 percent of the corporation's tax preferences in excess of the greater of the regular income tax paid or $10,000.

The tax preference items included in this base of the minimum tax for corporations are:

(1) Accelerated depreciation on real property in excess of straight-line depreciation over the useful life or recovery period;

(2) Amortization of certified pollution control facilities (the excess of 60-month amortization over depreciation otherwise allowable);

(3) In the case of certain financial institutions, the excess of the bad debt deductions over the amount of that deduction computed on the basis of actual experience;

(4) Percentage depletion in excess of the adjusted basis of the property;

(5) $^{18}/_{46}$ of the corporation's net capital gain; and

(6) Amortization of child care facilities (the excess of 60-month amortization over depreciation otherwise allowable).

House bill

No provision.

Senate amendment

The Senate amendment provides for a 15-percent cutback in certain corporate tax preferences. The changes apply to all corporations other than subchapter S corporations.

In the case of corporations, the statutory percentage depletion rates for iron ore and coal (including lignite) are reduced by 15 percent.

The bad debt reserve deduction is reduced by 15 percent of the amount by which the otherwise allowable deduction exceeds the amount which would have been allowable on the basis of actual experience.

In the case of a financial institution, 15 percent of the otherwise allowable interest deduction for debt incurred or continued to purchase tax-exempt obligations acquired after 1982 is disallowed.

The deemed dividend distribution by a domestic international sales corporation (DISC) to a corporate shareholder is increased by 15 percent, to 57½ percent of certain taxable income.

The amount treated as ordinary income on the sale of section 1250 property (real estate) by a corporation is increased by 15 precent of the additional amount which would be ordinary income if the property were subject to recapture under section 1245.

Fifteen percent of the basis of pollution control facilities to which an election under section 169 applies is treated as if the election did not apply.

In the case of an integrated oil company, 15 percent of the amount otherwise allowable as a deduction for intangible drilling costs under section 263(c) is capitalized to the oil, gas or geothermal property and treated as if it were recovery property assigned to the 5-year class. ACRS deductions and the investment tax credit are made available. The deductions and the credit are subject to recapture in accordance with the usual recapture rules. The deductions are also reduced to take account of the half-basis adjustment. Integrated oil companies may elect on an annual basis to capitalize up to 100 percent of otherwise allowable IDCs under these new rules.

Fifteen percent of the deductions for mining exploration and development costs otherwise allowable under section 616(a) and 617 to a corporation are capitalized and treated in generally the same manner as the capitalized IDC's described above.

Only 71.6 percent of the items subject to a cutdown will be treated as items of tax preference under the add-on minimum tax for corporations.

The provisions generally apply to taxable years beginning after December 31, 1982. However, the provision relating to deductions under secs. 263(c), 616 and 617 applies to expenditures made after that date; the provision relating to pollution control facilities applies to property placed in service after that date; the provision relating to section 1250 property applies to dispositions after that date; and the provision relating to depletion applies to taxable years beginning after December 31, 1983.

Conference agreement

The conference agreement follows the Senate amendment with several modifications: First, the preference for percentage depletion for coal and iron ore that is subject to the 15-percent cutback is defined as excess of percentage depletion otherwise allowable over the adjusted basis of the property. This replaces the Senate provision reducing the percentage depletion rates by 15 percent. Second, the treatment of the 15 percent of intangible drilling costs of integrated oil companies that is made ineligible for expensing is that these costs are written off over 36 months with no investment tax credit. Third, the Senate provision allowing corporations to elect not to expense more than 15 percent of intangible drilling and mining exploration and development costs is deleted. The present law election to capitalize intangible drilling costs is not changed. Fourth, the conference agreement removes rapid amortization for child care facilities as a minimum tax preference for corporations.

The conference agreement also makes a technical amendment relating to real estate investment trusts (REITs). Under present law, REITs are generally treated as conduit entities to the extent that their income (including capital gain) is distributed to its shareholders. However, a REIT is taxed like an ordinary corporation on income (including capital gain) it retains.

In order to continue this treatment with respect to the preference for section 1250 capital gain treatment, the conference agreement provides that the amount subject to the 15-percent ordinary income treatment is reduced by the amount of section 1250 capital gain which is distributed to shareholders and is designated as a capital gain dividend. For this purpose, capital gain dividends are deemed to be paid first from section 1250 capital gain. Thus, no section 1250 capital gain is treated as ordinary income where capital gain dividends for the year are more than the section 1250 capital gain. Any gain treated as ordinary income is considered as real estate investment trust taxable income.

Individual shareholders of a REIT continue to treat capital gain dividends as capital gains for purposes of the individual minimum tax. Corporate shareholders of a REIT treat the portion of the capital gain dividend attributable to gain from the sale or exchange of section 1250 property as subject to the 15-percent ordinary income rule. It is expected that the Internal Revenue Service will modify its regulations to require REITs to designate which portion of their capital gain dividends are paid from section 1250 capital gain and the amount of such gain that would be ordinary income if the property were subject to section 1245 recapture so that their corporate shareholders will know the amount of their preference for section 1250 capital gain treatment.

2. Basis adjustment for investment tax credits

Present law

Cost recovery deductions are allowed for 100 percent of the cost of a depreciable asset, including property for which the regular, energy, or historic structure rehabilitation investment tax credits are allowed. Basis is reduced by the full amount of rehabilitation credits except that no basis reduction is required for the credit for qualified rehabilitation of historic structures.

Lessors may elect to pass through investment credits to lessees, in which case lessees are treated as having purchased the asset for fair market value for purposes of computing the credit.

House bill

No provision.

Senate amendment

The Senate amendment requires a taxpayer to reduce the basis of assets by 50 percent of the amount of regular, energy and certified historic structure investment tax credits. This applies to credits claimed on qualified progress expenditures as well as on ordinary credits. A deduction also is allowed for one-half of unused credits in the year in which they expire. When a lessor elects to pass through the investment credit to a lessee, the lessor takes the basis adjustment. The basis adjustment is not taken into account in determining earnings and profits.

The amendment applies to property placed in service after December 31, 1982, other than property (which is not public utility property, property subject to a safe-harbor lease or a rehabilitated building) placed in service before July 1, 1984, for which a contract was entered into after August 13, 1981, and was binding on July 1, 1982, and at all times thereafter. For property placed in service after 1982 which is not covered by the transition rule, qualified progress expenditures and expenditures for property constructed by the taxpayer incurred before 1983 are not subject to the new rules.

Conference agreement

The conference agreement follows the Senate amendment with several modifications.

First, taxpayers are given an election with respect to the regular investment credit on recovery property to elect a 2-percentage point reduction in the credit. The election is made property by property. A taxpayer who makes this election does not have to make a basis adjustment. In the case of partnerships, the election is made at the partnership level. The election is intended to deal with the case in which a taxpayer cannot claim all the regular investment credits he earns because of the 85-percent-of-tax-liability limitation. In these cases, taxpayers could be forced to make a basis adjustment, and suffer a deferral of deductions for which they would have received a tax benefit, because they earn credits they will be able to use only after carrying them forward for several years. Under the conference agreement, these taxpayers are able to avoid this problem by electing the reduced credit.

Second, when lessors elect to pass through the investment credit to lessees under section 48(d), the lessor does not have to make a basis adjustment. Instead, the lessee includes in income ratably over the ACRS recovery period for the property an amount equal to one-half of the credit allowable. Lessees are eligible to elect the 2-percentage point reduction for the regular investment credit in which case they are not required to include this income. If the credit is recaptured, the income inclusions will be adjusted, in accordance with regulations, to take account of the amount of the credit recaptured.

Third, the conference agreement liberalizes the transition rules in the Senate amendment. The date by which property eligible for the transition rule must be placed in service in order to be exempt from the basis adjustment is extended from July 1, 1984, to January 1, 1986. Also, in the case of an integrated manufacturing facility where there were binding contracts, or where construction by the taxpayer was carried out with respect to more than 20 percent of the cost of the facility, between August 13, 1981, and July 2, 1982, and where the on-site construction began before July 1, 1982, property eligible for the credit in the facility will qualify for the transition rule if the property is placed in service before January 1, 1986.

An integrated manufacturing facility is one or more facilities located on a single site for the manufacture of one or more manufactured products from raw materials by the application of two or more integrated manufacturing processes. For example, an integrated facility for the manufacture of steel or steel products from raw materials would qualify as an integrated manufacturing facility.

Fourth, a transition rule is adopted for rehabilitation of certified historic structures. These are exempt from the basis adjustment if there is a contract to rehabilitate the property which was entered into after December 31, 1980, and was binding on July 1, 1982, and at all times thereafter or if rehabilitation began between December 31, 1980, and July 1, 1982, as long as the building is placed in service before January 1, 1986. Also, rehabilitations of certified historic structures placed in service before July 1, 1984, are exempt if Securities and Exchange Commission filings and HUD Section 8 applications with respect to those structures were made before July 1, 1982.

3. Limitation on investment tax credit

Present law

The investment tax credit earned by a taxpayer can be used to reduce tax liability up to certain limits. The limit for taxable years ending after 1981 is $25,000 plus 90 percent of the tax liability in excess of $25,000 (increased from 80 percent in 1981). Unused credits for a taxable year may be carried back to each of the 3 taxable years preceding the unused credit year and then carried forward to each of the 15 following taxable years.

House bill

No provision.

Senate amendment

The limitation on the amount of income tax liability (in excess of $25,000) that may be offset by the investment tax credit is reduced from 90 percent to 85 percent.

The lower limitation is effective for taxable years beginning after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment.

4. Accelerated depreciation (ACRS)—1985 and 1986

Present law

Cost recovery schedules for equipment reflect the 150-percent declining balance method with a switch to the straight-line method, for the years 1981–84. In 1985, the schedules accelerate to reflect the 175-percent declining balance method with a switch to the sum-of-the-years-digits method. In 1986, they accelerate further to reflect the 200-percent declining balance method with a switch to the sum-of-the-years-digits method.

House bill

No provision.

Senate amendment

The Senate amendment repeals 1985 and 1986 accelerations of depreciation.

Conference agreement

The conference agreement follows the Senate amendment.

5. Construction period interest and taxes

Present law

Under section 189, individuals, personal holding companies, and subchapter S corporations are required to capitalize interest and real property taxes attributable to the construction period of real property (other than low-income housing) to be used in a trade or business or held for investment. The capitalized interest and taxes are amortized (i.e., deducted in equal portions) over certain periods, generally 10 years. The interest that must be capitalized is interest which is attributable to the construction period on any debt incurred or continued for the purpose of acquiring, constructing, or carrying real property other than low income housing. The construction period is defined as the period beginning on the date construction of the building or improvement begins and ending on the date the property is ready to be placed in service or is ready to be held for sale.

The amortization of capitalized interest and taxes begins in the year the interest or taxes was paid or accrued. However, the amortization of capitalized interest and taxes is then suspended until the year the building or improvement is ready to be placed in service or to be sold, and amortization resumes at that time.

Corporations, other than personal holding companies and subchapter S corporations, are not subject to the capitalization requirement of section 189. For these corporations, amounts paid or accrued for interest and real property taxes are allowed as deductions for the year in which paid or accured. Certain prepaid interest, however, must be capitalized and deducted in the years to which properly applicable. In addition, under section 266, taxpayers may elect to capitalize certain taxes and interest attributable to both real and personal property and include the capitalized items in the basis of the property.

Section 189 does not apply to interest and taxes capitalized under section 266.

House bill

No provision.

Senate amendment

Section 189 generally would be extended to apply to all corporations. However, for corporations other than personal holding companies and subchapter S corporations, section 189 would not apply to construction period interest and taxes for residential real property. In addition, the Treasury Department would be required to issue regulations providing for the allocation of interest to the construction of real property, and it would be expected that these regulations would adopt rules similar to those contained in Financial

Accounting Standards Board Statement Number 34, as amended. Under those rules, the amount of interest to be capitalized is the portion of the total interest expense incurred during the construction period that could have been avoided if funds had not been expended for construction. Interest expense that could have been avoided includes interest costs incurred by reason of additional borrowings to finance construction and interest costs incurred by reason of borrowings that otherwise could have been repaid with funds expended for construction.

The Senate amendment generally would apply to interest and taxes paid or incurred in taxable years beginning after December 31, 1982, for the construction of nonresidential real property begun after December 31, 1982. The Senate amendment would not apply, however, to the construction of the Alaska Natural Gas Transportation System (15 U.S.C. 719) and its related facilities (e.g., compressor stations and conditioning plants). In addition, the Senate amendment would not apply to the construction of hotels or motels described in section 48(a)(3)(B) begun before January 1, 1984, if the construction is done under a written plan of the taxpayer in existence on July 1, 1982, and if the taxpayer has requested in writing approval from a governmental unit for such hotel or motel.

Conference agreement

The conference agreement follows the Senate amendment with one amendment to the effective date. Under the amendment, the special transitional rule of the Senate bill for hotel and motel construction is extended to apply also to the construction of hospitals and nursing homes.

The conferees understand that the construction period commences with the date on which the construction of a building or other improvement begins and ends on the date that the building or improvement is ready to be placed in service or is ready to be held for sale. For this purpose, the construction period is not to be considered to have commenced solely because drilling is performed to determine soil conditions, architect's sketches or plans are prepared, or a building permit is obtained. Generally the construction period will be considered to have commenced when land preparations and improvements, such as clearing, grading, excavation, and filling, are undertaken. However, the construction period will not be considered to have commenced solely because clearing or grading work is undertaken, or drainage ditches are dug, if such work is undertaken primarily for the maintenance or preservation of raw land and existing structures and is not an integral part of a plan for the construction of new or substantially renovated buildings and improvements. In the case of the demolition of existing structures where the construction period has not otherwise commenced, the construction period is considered to commence when demolition begins if the demolition is undertaken to prepare the site for construction. The construction period will not be considered to commence solely because of the demolition of existing structures if the demolition is not undertaken as part of a plan for the construction of new or substantially renovated buildings or improvements.

The conferees also intend to clarify that the construction of property is considered to have begun before January 1, 1983, if the property is an integral part of an integrated facility and construction of part of that facility began before January 1, 1983. An integrated facility is a multi-property facility constructed as a single project on a single site and operated as a single, unitary facility as described in a written plan (evidenced by internal documents of the taxpayer such as purchasing and financing documents) existing on July 1, 1982. Property is an integral part of an integrated facility if:

(1) the property is described as part of the same project in written plans of the taxpayer in existence on July 1, 1982;

(2) the property is an integral part the planned operation of the project when the project will first be placed in service; and

(3) the property will be constructed during the same construction period as the rest of the project.

Thus, for example, three nuclear reactors are not part of one integrated facility for the production of electricity if it is planned that only one reactor will be placed in service initially. On the other hand, if a taxpayer plans to construct a facility to produce sheet steel from iron ore, then both a blast furnace and rolling mill to be constructed during the same construction period on a single site are part of the same integrated facility because both properties are necessary to produce sheet steel from iron ore as contemplated in the taxpayer's plan. However, if the blast furnace is planned to be ready to be placed in service in 1985 and construction of the rolling mill is not planned to begin until 1986, then those properties are not part of one integrated facility.

Although improvements such as parking lots, access roads, and utility hook-ups may be part of an integrated facility, the start of construction of such property (which can be used in connection with any type of facility) is not considered the start of construction of other property in the facility for purposes of the effective date of the provision.

6. Leasing Rules

a. Non-safe harbor leasing rules

Present law

General concept

Prior to the enactment of ERTA, the law contained rules to determine who owns an item of property for tax purposes when the property is subject to an agreement which the parties characterize as a lease. These rules, which evolved over the years through a series of court cases and revenue rulings and revenue procedures issued by the Internal Revenue Service, still apply to transactions that are not governed by the safe-harbor rules. Essentially outside the safe harbor provided by ERTA, the law is that the economic substance of a transaction, not its form, determines who is the owner of the property for tax purposes. Lease transactions cannot be used solely for the purpose of transferring tax benefits. In general, that means that the lessor has to have a profit or income-producing motive for the transaction independent of tax benefits. Other business motives are taken into account in determining the substance of the transaction. The fact that the lessor in a lease financing transaction can show a profit or business purpose does not automatically result in lease treatment because a profit motive also can exist in a financing arrangement. In addition, the lessor has to bear meaningful benefits and burdens of ownership. The transaction has to be in substance a lease and not a financing arrangement or a conditional sale.

Objective guidelines (Revenue Procedure 75-21)

Revenue Procedure 75-21 and subsequent revenue procedures provide the following objective guidelines for determining non-safe harbor lease treatment of leveraged leases of equipment. These guidelines may be viewed as a type of safe harbor because if all requirements are met, a ruling generally will be issued treating the transaction as a lease.

1. *Lessor's minimum investment.*—The lessor must have a minimum 20 percent unconditional at-risk investment in the property.
2. *Lessee's investment.*—Neither the lessee nor a party related to the lessee may furnish any part of the cost of the property.
3. *Lessee loans or guarantees.*—The lessee may not lend to the lessor any of the funds necessary to purchase the property or guarantee any lessor loan.
4. *Purchase options.*—The lessee may not have an option to purchase the property at the end of the lease term unless the option can be exercised only at fair market value (determined at the time of exercise). In addition, the lessor cannot have a contractual right

to require the lessee or any other party to purchase the property, even at fair market value (i.e., a put).

5. *Lessor profit and cash flow.*—The lessor must expect to receive a profit and positive cash flow from the transaction independent of tax benefits.

6. *Limited use property.*—Under Revenue Procedure 76-30, property that can be used only by the lessee (limited use property) is not eligible for lease treatment.

Motor vehicle leases

One court (*Swift Dodge* v. *Commissioner,* 76 T.C. 546 (1981)) has held that, in an operating lease of motor vehicles, lease treatment may result even though the lease contains a terminal rental adjustment clause requiring or permitting an adjustment of rent to make up any difference between the projected value of the property at the end of the lease and the actual value of the property upon lease termination. The I.R.S. has not acquiesced in this case.

House bill

No provision.

Senate amendment

Fixed price purchase options

For leases entered into after December 31, 1984, fixed price purchase options are not to be taken into account in determining whether a transaction is a lease under the non-safe harbor rules. To qualify, the option must be at least 10 percent of the original cost of the property. As under present law, the fact the lessor has a contractual right requiring the lessee to purchase the property (i.e., a put option) in a lease must be taken into account in determining whether a transaction is a lease under non-safe harbor rules.

This change permitting a fixed price purchase option applies to certain leases of farm property entered into after July 1, 1982. To be eligible, the property must be new property eligible for the investment credit and used for farming purposes as defined in section 2032A(e)(5). A lease does not qualify if the cost basis of the leased property when added to the cost basis of all other property subject to a lease that was entered into by the lessee (or a related person) during the same calendar year and that was covered by this rule exceeds $150,000. For this purpose, a related person is defined in section 168(e)(4)(D), except that an individual is not considered related to the lessee individual if the property is used in a trade or business of farming that is separate from the trade or business of farming of the lessee.

Motor vehicle leases

The Senate amendment prevents the IRS from retroactively denying lease treatment for certain motor vehicle leases, including leases of trailers, by reason of the fact that those leases contain terminal rental adjustment clauses. The provision does not address the legal effect of these clauses and does not prevent the Treasury from issuing regulations on a prospective basis addressing the legal effect of these clauses.

The Senate provision regarding terminal rental adjustment clauses applies only to leases in which the lessee uses the property for business purposes. Also, the provision does not apply to leveraged leases financed with nonrecourse debt.

Other rules unchanged

The Senate amendment does not otherwise alter Revenue Procedure 75-21 or the general principles for determining lease treatment of transactions other than safe-harbor lease transactions.

Effective date

Fixed price purchase options.—In general, the change for fixed price purchase options applies to leases entered into after December 31, 1984. However, the provision for up to $150,000 of a lessee's farm property applies to leases entered into after July 1, 1982 and before January 1, 1985.

Motor vehicle leases.—The provision governing motor vehicle leases applies to any open taxable year.

Conference agreement

Overview

The conference agreement modifies the Senate amendment in several respects. Under the conference agreement, leases that qualify under the non-safe harbor rules are allowed the same 90-day window presently allowed for safe harbor leases. Thus, property subject to a non-safe harbor lease will be considered new property if it is leased within 90 days after the property is placed in service. In addition, the conference agreement establishes a new category of leases referred to as finance leases.

These rules generally apply to leases entered into after December 31, 1983. A special rule applies for finance leases entered into after July 1, 1982 of up to $150,000 of a lessee's farm property.

The conference agreement adopts without change the provision preventing the IRS from retroactively denying lease treatment to motor vehicle leases that contain terminal rental adjustment clauses. As under the Senate amendment, that change applies only to property that is used for business purposes and that is not financed with nonrecourse debt.

Finance leases

Overview.—Under the conference agreement, lease treatment is allowed for finance leases. A finance lease is an agreement characterized by the parties as a lease with respect to eligible property that would meet the requirements of a lease under the non-safe harbor rules if the fact that the agreement contained a 10-percent fixed price purchase option or that the property was limited use property were not taken into account in determining lease treatment. To be a finance lease, the lessor must be a corporation (other than a subchapter S corporation or a personal holding company), a partnership all partners of which are those corporations, or a grantor trust with respect to which the grantor and all beneficiaries are those corporations. Finance leases (other than finance leases of up to $150,000 of a lessee's farm property per calendar year) are subject to a lessee cap, a lessor cap, and an ITC spread. Limitations on related party transactions and percentage depletion deductions of lessees apply to all finance leases.

Eligible property.—Under the conference agreement, property eligible for finance lease treatment includes only recovery property that is new section 38 property. However, eligible property does not include public utility property (as defined in section 167(l)(3)(A)) or rehabilitated buildings. The conference agreement excludes property used by former tax-exempt organizations excluded from the safe-harbor provisions under the Senate amendment, except that the exclusion does not apply to property used by farmer's cooperatives described in section 521 (whether or not they are exempt from tax) or to property used in an unrelated trade or business, the income from which is subject to tax under section 511. In addition, property does not qualify if it is used by a person other than a U.S. person and that foreign user is not subject to U.S. tax on the income generated from the property. Mass commuting vehicles are not eligible.

10-percent fixed price purchase option.—A 10-percent fixed price purchase option means an option of the lessee (i.e., a call option) to purchase the property at the end of the lease term for a price that is fixed at the beginning of the lease term at an amount that is 10 percent or more of the original cost of the property.

Limited use property.—Limited use property is property that is not readily usable by any person other than the lessee.

Other non-safe harbor lease rules apply.—Finance leases must meet the requirements for lease treatment under non-safe harbor rules, disregarding the fact that the lease contains a 10-percent fixed price option or that the property is limited use property. Thus, the transaction must have economic substance independent of tax benefits and not merely be cast in the form of a lease for purposes of utilizing the lessor's tax base. The lessor must reasonably expect to derive a profit from the transaction independent of tax benefits. In addition to a profit, the transaction must not (without regard to the fact the agreement contains a fixed price option or that the property is limited use property) in substance be a financing arrangement or conditional sale in which the lessee has an investment in the property.

Investment tax credit.—Under the conference agreement, 20 percent of any investment credit earned for finance lease property is allowable in the first taxable year and 20 percent of the credit is allowable in each of the 4 succeeding taxable years. In computing cost recovery allowances for finance lease property, the regular ACRS periods and methods apply. The basis adjustment for half of the full investment credit occurs in the first taxable year.

This spreading of an investment credit does not apply to property placed in service after September 30, 1985.

Lessor limitations.—In taxable years ending after December 31, 1983, a lessor is not allowed deductions or credits allocable to finance lease property to the extent those deductions or credits reduce its income tax liability (including any liability under the add-on minimum tax) by more than 50 percent.

Deductions or credits not allowed by operation of this limitation may be carried forward, under regulations to be prescribed by the Secretary. This lessor limitation does not apply to property placed in service after September 30, 1985, in taxable years beginning after that date.

A lessor cannot use tax benefits from property in a finance lease to generate a net operating loss carryback or investment tax credit carryback to a prior taxable year. This rule operates in the same way as the rule prohibiting carrybacks (and allowing carryforwards) of tax benefits obtained under the safe-harbor lease provisions.

Lessee limitations.—The conference agreement places a 40-percent limit on the amount of a lessee's qualified base property that may be leased during any calendar year under a finance lease. Qualified base property includes new section 38 property of the lessee, financed lease property (other than new section 38 property of the lessee), and designated leased property. Designated leased property has the same meaning as in the lessee cap of the safe harbor provisions. Property leased last during the calendar year is considered to be the first property denied lease treatment under this rule. The lessee cap does not apply after calendar year 1985.

The conference agreement requires a lessee to compute its percentage depletion deduction for property subject to a finance lease as if it owned the property. In general, rules similar to the rules for the percentage depletion computation under the safe-harbor provisions of the Senate amendment apply in making this computation. However, the lessee must use the regular ACRS deductions allowed under the law in effect at the time of the lease agreement in making this determination rather than the modified ACRS deductions required for safe-harbor leases.

Related party transactions.—The finance lease rules do not apply to transactions between related persons. For this purpose, persons are related if they are part of an affiliated group as defined in section 1504 even if the persons are not an "includible corportation" (as defined in section 1504(b)) and even though the group does not file a consolidated return.

Farm finance leases.—Leases of new section 38 property used for farming purposes entered into after July 1, 1982, may qualify for finance lease treatment if the cost basis of the leased property when added to the cost basis of all other farm property subject to a finance lease that was entered into by the lessee (or a related person) during the calendar year does not exceed $150,000. A related person has the same meaning as under the Senate amendment. These leases of farm property are not subject to the lessor cap, the lessee cap, or the spread of the investment credit. However, those limitations apply for leases entered into after December 31, 1983, of property exceeding the $150,000 amount. The limitations on related party transactions and percentage depletion of a lessee apply to farm finance leases for all years.

Other non-safe harbor leases unaffected

The conference agreement does not alter the present law treatment of leases other than finance leases or safe harbor leases.

Effective dates

The provision permitting a 90-day window applies to leases entered into after December 31, 1983. The finance lease provisions also generally apply to property placed in service after December 31, 1983. However, the rules relating to finance leases of up to

$150,000 of a lessee's farm property apply to leases entered into after July 1, 1982. The motor vehicle provisions apply to any open taxable years.

b. Safe-harbor leasing rules

Present law

General concept

The safe-harbor leasing provisions of ERTA are intended to permit owners of property to transfer the tax benefits of ownership (depreciation and the investment credit) to other persons without having to meet the prior law requirements for characterizing the transaction as a lease. The safe-harbor leasing provisions operate by guaranteeing that for Federal tax purposes qualifying transactions will be treated as leases, and that the nominal lessor will be treated as the owner of the property, even though the lessee is in substance the owner of the property and the transaction otherwise would not be considered a lease.

Eligibility requirements

Maximum lease term.—The lease term may not exceed the greater of 90 percent of the useful life of the property or 150 percent of the ADR midpoint of the property.

Maximum interest rate on lessee obligations.—Under Treasury regulations, the rate may not exceed by more than 3 percentage points the rate on tax overpayments and underpayments, the prime rate, or an arms-length rate determined under section 482.

Eligible property

General rule.—Property must be "qualified leased property," which, in general, means that the property must be new equipment eligible for both ACRS and the investment credit.

90-day window.—The equipment may be leased within 3 months after the property is placed in service without violating the requirement that the equipment be new equipment (called the 90-day window).

Property used by tax-exempt organizations.—Property (other than mass commuting vehicles) used by a tax-exempt organization or a U.S. Federal, State, or local government unit generally is ineligible.

Mass commuting vehicles.—Qualified lease property includes mass commuting vehicles (which means any bus, subway car, rail car or similar equipment that is leased to a governmentally owned mass transit system and used in providing mass commuting services) that are financed in whole or in part by tax-exempt bonds.

Public utility property.—Public utility property is eligible for the safe-harbors rules.

ACRS deductions

Recovery period.—The taxpayer may elect the regular ACRS recovery period of 3 years for 3-year property, 5 years for 5-year property and 10 years for 10-year property.

Recovery method.—The taxpayer may elect accelerated percentages approximating use of the 150-percent declining balance method in early recovery years and the straight-line method in subsequent recovery years.

Investment tax credit.—100 percent of any investment tax credit is allowable when property is placed in service.

Related party transactions

The Treasury regulations governing the safe harbor rules reserved on whether transactions between related parties qualify for safe-harbor treatment.

ITC strip

The Treasury regulations reserved on whether safe-harbor lease treatment is allowed for transactions referred to as lease-leasebacks or ITC strips intended to permit the lessee to transfer only the investment credit.

Closely-held lessors

The at-risk limitations on losses (sec. 465) and credits (sec. 46(c)(8)) may apply where a closely-held corporation is either a lessor or lessee. In general, to be at-risk, the taxpayer must use cash or recourse debt to finance the property.

House bill

No provision.

Senate amendment

Eligibility requirements

Maximum lease term.—The lease term cannot exceed 100 percent of the present class life (ADR midpoint as of January 1, 1981) of the property (generally 9 years for property without an ADR life).

Interest rate.—The interest rate may not exceed the rate of overpayments and underpayments of tax reduced by 5 percentage points, but not below 8 percent.

Eligible property

General rule.—The definition of qualified leased property eligible for the safe-harbor is generally the same as under present law. However, public utility property is not qualified leased property under the Senate amendment.

Property used by tax-exempt organizations.—Qualified leased property will not include property (other than mass commuting vehicles) leased to a person that was a tax-exempt organization at any time within the 5-year period preceding the date of the lease agreement. This rule also applies where a predecessor of the lessee, within the 5-year period prior to the date the lease is entered into, was a tax-exempt organization and was engaged in activities substantially similar to the activities in which the lessee is engaged.

Mass commuting vehicles.—In general, the definition of mass commuting vehicles eligible for the safe harbor is the same as under present law. However, ferries are specifically designated as mass commuting vehicles.

ACRS deductions

Recovery period.—Recovery periods are 5 years for 3-year property, 8 years for 5-year property and 15 years for 10-year property.

Recovery method.—The recovery method is the straight-line method (with a half-year convention).

Investment tax credit.—Any investment tax credit earned on leased property is allowable over 3 years—50 percent the first year and 25 percent in each of the next 2 years. However, the half-basis adjustment takes effect the first year.

Lessee limitations

Cap on eligible property.—The lessee may apply the safe-harbor rules with respect to no more than the following percentages of the lessee's qualified base property placed in service during any calendar year:

Year	*Percent*
1982	45
1983	45
1984	40
1985	40

Qualified leased property not subject to this provision by virtue of the general effective date or transitional rules counts toward the lessee cap in 1982, but the rule does not operate to deny safe-harbor lease treatment for that property.

For this purpose, the lessee's qualified base property includes (1) the cost basis of all qualified leased property leased by the lessee under a lease for which a safe-harbor election has been made, (2) all other new section 38 property of the lessee that is placed in service during the taxable year, and (3) designated lease property, which is new property eligible for the investment credit that is used by the lessee under a long-term (more than 50 percent of the ADR midpoint of the property) agreement qualifying as a lease under non-safe harbor rules.

Property leased last during the calendar year is considered to be the first property denied lease treatment under this rule.

Percentage depletion.—The lessee must compute its 50-percent and 65-percent taxable income limitations on percentage depletion deductions as if it were the owner of the leased property. For this purpose, the lessee must take into account ACRS deductions for the property and must disregard lease rentals and interest on lessee financing. In computing the imputed ACRS deductions for the property, the lessee must use the recovery period and method applicable to the lessor under the new safe-harbor rules.

Foreign tax credit.—The lessee must compute its foreign tax credit as if the lessee were the owner of the property. Thus, it must take into account ACRS deductions (and disregard rentals and interest on lessee financing) computed using the periods and methods applicable to the lessor.

Lessor limitations

Current tax liability.—In taxable years ending after July 1, 1982, a lessor is not allowed deductions or credits allocable to qualified leased property to the extent those deductions or credits reduce its income tax liability (including any liability under the add-on minimum tax) by more than 50 percent. Thus, the lessor's tax liability is the greater of (1) tax computed by taking into account ACRS deductions, investment credits, rentals, and interest or lessee financing allocable to qualified leased property or (2) 50 percent of the tax computed without taking into account those items. Deductions or credits from safe-harbor leases not allowable by operation of this rule may be carried forward under regulations to be prescribed by the Secretary. No deferral of tax benefits is required with respect to deductions or credits arising from safe-harbor leases not covered by the Senate provisions, but such deductions or credits count first in determining whether the 50-percent limitation applies to safe-harbor leases covered by the Senate provisions.

Carrybacks.—A lessor cannot use tax benefits obtained as a safe-harbor lessor to generate a net operating loss carryback or investment tax credit carryback to a prior taxable year. In determining the amount of any carryback, taxable income or tax liability must be reduced first by tax benefits that are not attributable to safe-harbor leases. The Senate amendment does not prohibit a carryover of these amounts.

Related party transactions

The Senate amendment prevents the lessee from entering into a safe-harbor lease with a related person. For this purpose, persons are related if they are part of an affiliated group as defined in section 1504, even if the persons are not "includible corporations" (as defined in section 1504(b)) and even though the group does not file a consolidated return.

ITC strip

The Senate amendment allows safe-harbor lease treatment for transactions referred to as lease-leasebacks or ITC strips entered into before October 20, 1981, which is the date Treasury issued its temporary regulations dealing with the safe-harbor provisions.

Closely-held lessors

Under the Senate amendment, the at-risk limitations on losses and credits generally do not apply to lessors that are closely-held corporations with respect to qualified leased property for which a safe-harbor election has been made. If the lessee would be treated as the owner without regard to the safe-harbor rules, the at-risk rules will apply to closely-held lessors to the extent those rules would apply to the lessee. Also, the at-risk rules will continue to apply to closely-held corporations the principal function of which is the performance of services in the field of health, law, engineering, architecture, accounting, actuarial science, performing arts, athletics, or consulting.

Effective dates

General rule.—The Senate amendment generally applies to leases entered into or property placed in service after July 1, 1982, except the limitation on lessees relating to percentage depletion and the limitation on related party transactions apply to leases entered into after February 19, 1982.

Transition rule.—In general, the Senate provision does not apply if (1) the property is placed in service before July 1, 1983, and (2) after June 25, 1981 (the date H.J. Res. 266, which contained the safe-harbor leasing provisions, was ordered to be reported by the Senate Finance Committee) and before February 20, 1982, (a) the property was acquired by the lessee or construction of the property was commenced by or for the lessee or (b) the lessee entered into a binding contract for the purchase or construction of the property. For this purpose, a contract is not binding unless the lessee's failure to perform would subject him to liability for damages in an amount equal to or greater than 5 percent of the cost of the property.

Aircraft qualify under the transitional rule if the property is placed in service before January 1, 1984, and construction of a subassembly commenced or the stub wing join occurred between June 25, 1981, and February 20, 1982.

The June 25, 1981, date in the transitional rule is moved back to March 31, 1981, for paper production plants. Certain automobile manufacturing property qualifies under the transitional rule if placed in service before July 1, 1982 and leased before August 15, 1982.

Mass commuting vehicles.—The Senate provisions which modify the safe-harbor rules generally do not apply to mass commuting vehicles placed in service before January 1, 1988, pursuant to a binding contract or commitment entered into before April 1, 1983.

Repeal of safe-harbor leasing.—Safe-harbor leasing is repealed for property (other than mass commuting vehicles eligible under the special rule above) placed in service after September 30, 1985.

Conference agreement

Eligibility requirements

Maximum lease term.—The maximum lease term is the recovery period (described below) applicable to property in a safe-harbor lease or, if greater, 120 percent of the present class life of the property.

Interest rate.—Under the conference agreement, the interest rate on lessee obligations under a safe-harbor lease may not exceed the rate on overpayments and underpayments of tax.

Eligible property

General rule.—The general definition of qualified leased property is the same as under the Senate amendment.

Property used by tax-exempt organizations.—In general, the conference agreement adopts the provision in the Senate amendment excluding certain former tax-exempt organizations from qualified leased property. However, the conference agreement does not exclude from eligible property any property used by a tax-exempt organization in an unrelated trade or business the income from which is subject to tax under section 511. Also, farmers cooperatives described in section 521 are eligible for safe-harbor leasing whether or not they are exempt from tax.

Property used by certain foreign persons.—Under the conference agreement, qualified lease property does not include property used by a person other than a U.S. person if the income from use of the asset by that person is not subject to U.S. tax.

Mass commuting vehicles.—The conference agreement clarifies the Senate amendment regarding ferries to insure that property other than ferries does not qualify unless it is used to provide mass commuting services. For example, mass commuting vehicles do not include school buses.

ACRS deductions

Recovery period.—The conference agreement follows the Senate amendment.

Recovery method.—Cost recovery allowances are determined by applying prescribed percentages to the unadjusted basis of the property. These percentages are based on the 150-percent declining balance method, changing to the straight-line method, and using a half-year convention in the first recovery year. The percentages are set forth in the following table:

If the recovery year is:	The applicable percentage for the class of property is:		
	3-year	5-year	10-year
1	15	9	5
2	25	17	10
3	20	14	9
4	20	12	8
5	20	12	7
6		12	7
7		12	6
8		12	6
9			6
10			6
11			6
12			6
13			6
14			6
15			6

Investment tax credit.—The conference agreement generally follows the Senate amendment, except only 20 percent of an investment tax credit is allowable in each of the first five taxable years.

Lessee limitations

Eligible property.—In general, the conference agreement follows the Senate amendment. However, because the safe-harbor provisions do not apply after 1983, the lessee cap imposed by the Senate amendment in 1984 and 1985 does not apply. In addition, the conference agreement makes clear that property not subject to the modifications of the safe-harbor rules by virtue of the general effective date or transition rules counts towards computation of the lessee cap in 1983 as well as 1982.

Percentage depletion.—The conference agreement follows the Senate amendment.

Foreign tax credit.—The conference agreement deletes the limitation on the foreign tax credit for safe-harbor lessees.

Lessor limitations

The conference agreement follows the Senate amendment.

Related party transactions

The conference agreement follows the Senate amendment.

ITC strip

The conference agreement generally follows the Senate amendment.

Closely held lessors

The conference agreement generally follows the Senate amendment excluding closely-held lessors (other than personal service companies) from the at-risk rules for qualified leased property for which a safe-harbor election is in effect. However, the conference agreement extends the application of the rule to safe harbor leased property placed in service before the effective date where the lessor first becomes a closely held corporation after the general effective date. The conference agreement makes clear that the at-risk limitations also will not apply to closely held lessors with respect to safe harbor leased property that is not covered by the modifications to the safe-harbor provisions by virtue of the general effective date or transitional rules. The rules permitting closely held lessors to avoid application of the at-risk rules do not apply with respect to finance leases or other non-safe harbor leases.

Effective dates

General rule

The modifications to the safe-harbor leasing rules generally apply to leases entered into or property placed in service after July 1, 1982, except that the limitation on lessees relating to percentage depletion and the limitation on related party transactions apply to leases entered into after February 19, 1982.

Transitional rules

General rule.—Under the conference agreement, the modifications to the safe-harbor leasing provisions do not apply for property placed in the service before January 1, 1983 if after December 31, 1980 and before July 2, 1982 either (1) the property was acquired by the lessee or construction of the property was commenced by or for the lessee, or (2) a binding contract to acquire or construct the property was entered into by the lessee. For this purpose, a contract is not binding unless the lessee's failure to perform would subject him to liability for damages in an amount equal to or greater than 5 percent of the cost of the property.

Mass commuting vehicles.—The modifications to the safe-harbor leasing provisions do not apply to a mass commuting vehicle placed in service before January 1, 1988. In addition, these modifications do not apply to a mass commuting vehicle placed in service after December 31, 1987, if (1) the property was not placed in service before January 1, 1988, solely because of conditions that are not within the control of the lessor or lessee, and (2) the property was placed in service pursuant to a binding contract or commitment entered into before April 1, 1983. The definition of a binding contract or commitment for mass commuting vehicles is the same as under the Senate amendment.

Aircraft.—Under the conference agreement, the modifications to safe-harbor leases do not apply to commercial passenger aircraft (other than helicopters) placed in service before January 1, 1984, if after June 25, 1981, and before February 20, 1982, either (1) the property was acquired by the lessee or construction or reconstruction was commenced by or for the lessee, or (2) a binding contract to acquire or construct the property was entered into by the lessee. For this purpose, construction is considered to have commerced if construction of a subassembly was commenced or the stub wing join occurred. Construction of a subassembly means the joining of two or more separate parts to form an assembly by welding, riveting, bolting, or by other standard fastening methods in airframe or engine manufacturing procedures, including, but not limited to, bonding of fiberglass or graphite composites. Subassemblies may be built singly or in lot increments. The stub wing join occurs when the center wing section of the aircraft is joined with the right- and left-hand wings.

Auto manufacturing property.—The conference agreement adopts the Senate amendments that excludes certain automobile manufacturing property placed in service before July 1, 1982 and leased before August 15, 1982 from the modifications to safe-harbor leasing. In addition, the conference agreement excludes from the modifications to safe-harbor leasing automobile manufacturing property that would meet the requirements of the general transitional rule above if October 1, 1983 were substituted for January 1, 1983.

Steel.—The modifications to the safe harbor leasing provisions do not apply to proprty used by the taxpyer directly in connection with the trade or business of the manufacture or production of steel and placed in service before January 1, 1984, if after December 31, 1980, and before July 2, 1982, (1) the proprty was acquired by the taxpayer or construction of the property was commenced by or for the taxpayer, or (a) a binding contract was entered into for the property.

Boilers and turbines of certain cooperatives.—Under the conference agreement, the modifications to the safe-harbor leasing provisions do not apply for turbines and boilers placed in service by a cooperative organization described in section 1381(a) before July 1, 1983, if after December 31, 1980 and before July 2, 1982, at least 20 percent of the cost of the turbines or boilers was paid by the taxpayer.

The conferees understand that some lessees may have acquired various components before July 2, 1982, pursuant to contracts entered into before January 1, 1981. If those components are installed by the employees of the taxpayer after July 1, 1982, the property will qualify if the property is placed in service before January 1, 1983.

Definition of construction.—For purposes of the transitional rules, construction is considered to have commenced when physical work on construction of the property commences. Physical work does not include planning, research, design, engineering studies, securing financing, test drilling, or any other activity that does not involve physical work. Clearing land constitutes commencement of physical work on construction.

Property-by-property determination.—The transitional rules are applied for each separate item of property. For example, commencement of construction of a machine that will be placed in service in a plant commences when physical work on that machine begins. Commencement of construction of the machine is not considered to be commencement of construction of any other property in the plant. Similarly, the transitional rules regarding acquisitions and binding contracts apply for each separate item of property.

Repeal

The conference agreement repeals the safe-harbor lease provisions for leases entered into after December 31, 1983.

7. Foreign Tax Provisions

a. Limitation on amount of foreign oil and gas extraction taxes allowed as foreign tax credits

Present law

The amount of foreign oil and gas extraction taxes that may be credited is limited to an amount based on the U.S. corporate tax rate. However, to determine the credit, extraction losses from one country do not offset extraction income from other countries. Carryovers and carrybacks for excess extraction taxes paid are limited to 2 percent of foreign oil extraction income. The foreign tax credit limitation is computed separately for oil related income and all other foreign income.

If a taxpayer sustains an overall foreign loss in any taxable year, the taxpayer in succeeding taxable years must treat foreign source taxable income as U.S. source income in an amount which is equal to the lesser of (1) the remaining balance of the overall foreign loss, or (2) 50% of the taxpayer's taxable income from foreign sources for the succeeding taxable year in question. (Section 904(f), added to the Code in 1976.) The overall foreign loss must be determined separately for foreign oil and non-oil related income.

House bill

No provision.

Senate amendment

The Senate amendment changes the extraction loss rule so that a net extraction loss from one country offsets extraction income from other countries for the purpose of computing the amount of creditable oil and gas extraction taxes. The 2-percent limit on carryovers and carrybacks and the separate oil related income limitation are repealed. Credits are disallowed to the extent that foreign countries impose abnormally higher taxes on oil than on other activities. Also, the Senate amendment provides transitional rules dealing with carrybacks and carryforwards of credits. Under these transitional rules, pre-1983 overall foreign non-oil losses would cause the taxpayer to treat post-1982 overall foreign oil related income as U.S. source income. The Senate amendment applies to taxable years beginning after December 31, 1982.

Conference agreement

The conference agreement generally follows the Senate amendment, but adds a special rule to prevent the immediate recapture of non-oil related overall foreign losses. For this purpose, this special rule maintains the distinction between non-oil related and oil related overall foreign losses incurred in taxable years beginning before January 1, 1983, and subject to recapture in taxable years beginning after December 31, 1982. However, in order to assure that this special rule does not have an indefinite life, a provision to phase-in the recapture of any pre-1983 overall foreign non-oil related losses over a period of 8 years (generally, at a rate of 12½% a year) has been included in the Act. This special rule provides that in computing the recapture of an overall foreign non-oil related loss incurred in a taxable year beginning before 1983, the separate foreign tax credit limitation for non-oil related income as in effect under present law will generally apply. However, for purposes of applying the foreign tax credit foreign loss recapture rules with respect to taxes paid or accrued in a taxable year beginning after December 31, 1982, an additional amount of pre-1983 non-oil related income will be recaptured. This additional amount shall at least be equal to the lesser of: (1) an amount equal to 12½% of such pre-1983 overall foreign non-oil related loss multiplied by the number of taxable years that have elapsed since January 1, 1983, but less the amounts (if any) previously recaptured under the 12½% rule; or (2) the taxpayer's taxable income from sources without the United States that is not recaptured under the separate limitation rule above.

The conference agreement also changes the Senate amendment transitional rule for carryforwards of foreign tax credits from pre-enactment years.

It is the understanding of the conferees that the Department of the Treasury is to review the impact and effect of the foreign oil and gas tax credit provisions of the conference agreement on multinational oil companies and report its conclusions to the Congress by December 1, 1983.

b. Current taxation of foreign oil and gas non-extraction income

Present law

Income of a foreign corporation from foreign sources generally is not subject to U.S. taxation when earned. U.S. shareholders of a foreign corporation may be taxed on the income of a foreign corporation from certain tax haven or tax avoidance transactions under the anti-avoidance provisions of the Code (such as subpart F).

House bill

No provision.

Senate amendment

Under the Senate amendment, a new category of subpart F income would be added with respect to foreign oil and gas related income. Under this provision, U.S. shareholders of a controlled foreign corporation would be subject to tax currently on the foreign oil related income of the controlled foreign corporation from countries other than those in which the oil and gas is extracted or consumed. Foreign oil related income includes income from processing, transportation, distribution and sales, and services. Services are covered only if the provider is engaged in extraction. The other items are subject to tax currently even though neither the earner of the income nor a related party has extraction income. This provision would apply to taxable years of foreign corporations beginning after December 31, 1982, and to taxable years of United States shareholders in which or with which such taxable years of foreign corporations end.

Conference agreement

The conference agreement generally follows the Senate amendment, but clarifies one point and modifies another. The conference agreement makes it clear that fuel transferred into the fuel tank of a vessel or an aircraft (e.g., bunkers with respect to a vessel) for consumption by such vessel or aircraft is considered to be consumed in the country in which that transfer occurs.

In addition, the conference agreement exempts the U.S. shareholder of a controlled foreign corporation from current tax if neither the controlled foreign corporation nor any related person (as defined in Subpart F) has foreign oil or gas extraction income. The exemption will apply if the aggregate average daily production of foreign crude oil and natural gas by the foreign corporation and related persons for any taxable year is less than 1000 barrels per day (or its equivalent in gas).

c. Possession and Virgin Islands corporations

Present law

To qualify for effective tax exemption, a U.S. corporation must derive at least 50% of its gross income from the active conduct of a trade or business within a U.S. possession. Also, 80% of its gross income must be from possessions sources.

Possessions corporations (sec. 936) and certain U.S. corporations that are inhabitants of the Virgin Islands are, in general, effectively tax exempt. This exemption applies to income from intangibles created by such a corporation or acquired from an unrelated party. Taxpayers allege that an intangible asset (a patent, trademark, etc.) created by a related party and transferred to a possessions corporation generates tax-free income of the possessions corporation. The Internal Revenue Service allocates income from such an intangible to the related party. The issue is currently being litigated in the United States Tax Court.*

House bill

No provision.

Senate amendment

The required percentage of active business income for qualification for effective tax exemption is phased up to 90% for taxable years beginning in 1985 and thereafter. The percentage for 1983 is 65%; for 1984, 80%. Failure of the qualification tests because of IRS reallocation of intangibles income to other persons may be cured by distributions of disqualifying income. These distributions do not qualify for the dividends received deduction. Income from intangibles created by related parties is generally allocated to U.S. shareholders pro rata as U.S. source income. If a shareholder is a foreign person or a tax-exempt U.S. person, the possessions corporation (or V.I. corporation) is taxable on that shareholder's pro rata amount of the income from those intangibles as U.S. source income. Income from intangibles does not include a reasonable profit (as determined by the Secretary) on direct and indirect costs.

The provisions generally apply to taxable years beginning on or after January 1, 1983. They apply to a disposition on or after July 1, 1982 to a related party of an intangible asset that had been acquired from a related party.

Conference agreement

The conference agreement follows the Senate amendment with significant modification.

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*No inference should be drawn from this report or from the actions taken in the conference agreement that the conferees agree or disagraee with either the taxpayer involved or the Internal Revenue Service about this issue.

The provision as modified is intended to lessen the abuse caused by taxpayers claiming tax-free income generated by intangibles developed outside of Puerto Rico. The conferees also intend that the provision be administered in a fashion so as to encourage increased Puerto Rican employment and investment in depreciable property at as low a cost to the Treasury as possible.

The conferees are concerned about Puerto Rican job creation, and there is continuing concern that the provision may not be adequately targeted towards that goal. The conferees intend that the Treasury annual reports on section 936 address this question in detail. The conferees intend that the Treasury also consider in its annual reports whether a return attributable to intangible property might better encourage additional jobs and investment in Puerto Rico if it were measured by reference to costs of labor and capital located in Puerto Rico.

The conferees understand that there is concern that certain taxpayers who have been permitted by the Internal Revenue Service to use the cost-plus method of pricing without reflecting a return from intangibles but including the cost of materials in the cost basis would be precluded from doing so under the Senate bill. (Sec. 3.02(3) Rev. Proc. 63-10, 1963-1 C.B. 490.) The conferees do not intend any change in current treatment with respect to those taxpayers appropriately applying the cost-plus method. Accordingly, the Internal Revenue Service may continue in appropriate cases to permit such taxpayers to report their income as they have been under existing procedures.

Passive income

The percentage of a corporation's gross income that must be derived from the active conduct of a trade or business in a possession is increased from 50 percent to 65 percent. This increase will be phased in over three years. For taxable years beginning after December 31, 1982, the percentage limitation will be 55 percent, for taxable years beginning after December 31, 1983, the percentage limitation will be 60 percent, and thereafter the percentage limitation will be 65 percent.

Intangible income

An election may be made to treat income attributable to certain intangible property as income of the section 936 corporation eligible for the credit (and certain domestic corporations operating in the Virgin Islands) under two options—(1) a cost sharing rule and (2) a 50/50 profit split. The two exceptions with respect to certain types of intangible property found in the Senate amendment are deleted. In addition, an exception to the Senate bill is made for intangible property which has been licensed since prior to 1948 to a U.S. corporation operating in a possession and is in use by such corporation on the date of enactment.

Cost sharing

In general

A U.S. parent or other U.S. affiliate (collectively, "mainland affiliate") will be permitted to transfer certain manufacturing intangibles to its U.S. subsidiary or affiliate operating in a U.S. possession ("island affiliate"), provided the island affiliate (1) shares, through a cost sharing payment, in the annual product area research expenditures of the mainland affiliates and other affiliates controlled within the meaning of section 482 (collectively, "affiliates"), and (2) has a significant business presence in the possession. If these conditions are satisfied, the island affiliate will be deemed to own such manufacturing intangibles and will be entitled to the full return thereon with respect to the products produced or type of services rendered by the island affiliate. The applicable pricing methods provided in the section 482 regulations will be utilized for this psurpose. An island affiliate which makes the election will not be classified as a contract manufacturer with respect to the manufacturing intangibles. All other intangibles, such as marketing intangibles (including trademarks, trade names, and brand names) cannot be transferred to the island affiliate under this election, with the result that, for purposes of this election, the island affiliate cannot claim a return on such intangibles.

Manufacturing intangibles

The manufacturing intangibles covered by this election and with respect to which the island affiliate may claim a return must be related to the products produced or services rendered by the island affiliate.

Manufacturing intangibles will include patents, inventions, formulas, processes, designs, patterns, and know how. Even when marketing intangibles are closely associated with a specific manufacturing intangible, the return on the marketing intangible cannot be claimed by the island affiliate.

Cost sharing payment

The cost sharing payment will be equal in amount to a fraction of the current year's worldwide direct and indirect product area research expenditures. The fraction would generally equal the ratio of third party sales of products produced or services rendered, in whole or in part, in the possession to third party sales of all products produced or services rendered by the island affiliate and its affiliates (U.S. and foreign) in the same product area. The product area will be defined by reference to the three-digit classification of the Standard Industrial Classification ("SIC") code, or such other classification system as may be specified by the Secretary. The Secretary may provide rules for the aggregation of two or more three-digit categories in appropriate circumstances. An election of the cost sharing method is available even if no cost sharing payment is required (e.g., because of the absence of product area research expenditures).

(1) Multiplicand: product area research expenditures

Product area research expenditures, which will be defined on a three-digit SIC Code basis (or other classification system specified by the Secretary), are broadly defined and include both direct and indirect expenses (including expenses described in section 174) and a proper allowance of amounts expended for the acquisition or use of manufacturing intangibles and for the performance of research and development by another person, including qualified research expenses within the meaning of section 44F(b). They also include the costs of developing and purchasing research and development-related computer software.

Product area research expenditures will be determined on the basis of the product area for each activity in which the island affiliate conducts operations. The multiplicand will be computed on an annual basis and will include product area research expenditures in that product area which are incurred by the island affiliate and all affiliates (U.S. and foreign). Product area research expenditures incurred solely by the island affiliate in a taxable year (excluding amounts paid directly or indirectly to or on behalf of related persons and excluding amounts paid under any cost sharing agreement with related persons) will be offset against the amount of the cost sharing payment required to be made by the island affiliate for that year.

(2) Limiting Fraction: third party sales

(i) Numerator: possession sales.—The numerator of the fraction will be computed with reference to the products produced, and services rendered, in whole or in part, in the possession that are in the same product area used in the multiplicand. Sales in the numerator consist of sales of products produced in whole or in part (and services rendered) and sold by the island affiliate to third parties, and sales of products produced, and services rendered, by the island affiliate and sold by any U.S. or foreign affiliate to third parties. Thus, inter-affiliate sales are eliminated for this purpose.

(ii) Denominator: total sales.—The denominator of the fraction will also be computed with reference to the same product area used in the multiplicand. Sales in the denominator consist of all sales in the same product area to third parties by the island affiliate and all U.S. and foreign affiliates. For this purpose, inter-affiliate sales are eliminated.

Significant business presence

For an island affiliate to be eligible to elect cost sharing for a product or type of service, it must have and maintain a significant business presence in the possession with respect to that product or type of service. This test is intended to require real and significant business activity in the possessions.

The island affiliate satisfies this requirement with respect to a product or type of service if (1) more than 25 percent of the value added by the affiliated group to the product is added by the island affiliate in a possession or (2) at least 65 percent of the direct labor costs of the affiliated group for the product or service (or in connection with the purchase and sale of goods not produced by the affiliated group) are incurred by the island affiliate and are compensation for services rendered in the possession. In general, the figures to be used for these calculations will be those used by the island affiliate and its affiliates in their required inventory calculations. The Secretary may prescribe regulations providing significant business presence tests for other appropriate cases (including a value added test for services), which are consistent with the statutory tests.

The significant business presence test is not required to be satisfied for taxable years beginning before January 1, 1986 for any product produced or type of service rendered in a possession by the island affiliate on the date of enactment. The Secretary may prescribe regulations to provide a transitional (up to 3-year) significant business presence test for future start-up operations of new electing corporations and future possession products and possession services of an existing island affiliate. Regulations will provide definitions of a product or type of service and rules for dealing with components in the context of the foregoing requirements. If the significant business presence test is not satisfied for a product or type of service within the product area covered by the election, the cost sharing payment will not be reduced, and the provisions of the Senate amendment will apply to that product or type of service.

It is intended that the regulations will define the term "product" narrowly. In this manner the significant business threshold test will be more readily satisfied than if a broader definition applied, with the consequence that the income attributable to a product that satisfied the test will be computed with respect to that narrowly defined product.

Similarly, it is intended that components purchased by an island affiliate from an affiliate will be treated as materials (and the costs thereof as a cost of materials) where there is an independent resale price for such components or other factors are present such that the proper arm's length price of the components can be readily determined and such treatment is consistent with the intent of the significant business presence tests.

The Secretary will prescribe regulations providing for appropriate treatment in cases where the island affiliate purchases a component produced by an affiliate or produces a component which it sells to an affiliate for incorporation into a product sold to third parties.

Effect of cost sharing

For U.S. tax purposes, the cost sharing payment will not result in additional gross income to the mainland affiliate or affiliates, but will instead reduce the mainland affiliates' deductions for product area research expenditures and, to the extent necessary, other tax deductions. The credit for increasing research activities under section 44F will not be reduced by reason of the cost sharing.

Effect of electing to make cost sharing payments

If an election is made to use the cost sharing option, manufacturing intangibles covered by the election which are connected with the goods produced, or services rendered, in whole or in part, in the possession will, for purposes of the pricing rules discussed below, be deemed to be owned by the island affiliate, and the island affiliate will be entitled to the full return thereon.

Manufacturing intangibles developed solely by the island affiliate in a possession and owned by it, or acquired by the island affiliate from an unrelated party, will also be treated as owned by it for purposes of the pricing rules. For the purpose of determining when the island affiliate will be considered to have developed an intangible, rules (the "developer rules") similar to certain of the rules of the section 482 regulations will be provided, but an intangible developed under a cost-sharing agreement shall not qualify as developed solely by the island affiliate.

Nonmanufacturing intangibles

If the cost sharing rule is elected, all other intangibles (including those purported to have been transferred to the island affiliate) will not be treated as owned by the island affiliate for purposes of the intercompany pricing rules; and the island affiliate will not be entitled to any return thereon unless such intangibles are developed solely (within the meaning of the developer rules) by the island affiliate in a possession and owned by it. A further exception will apply in the case of sales made directly by the island affiliate to unrelated third parties for ultimate use or consumption in the possession, in which case the island affiliate will be entitled to the return on marketing intangibles developed by, or transferred by an affiliate to, the island affiliate.

Manufacturing intangibles and nonmanufacturing intangibles are defined according to lists of types of assets. Where an intangible is of a type which fits into two categories, e.g., a system, program, procedure or technical data (all defined as nonmanufacturing intangibles) which is also an invention, formula, process, design, pattern or know-how, it should be classified as a manufacturing or a nonmanufacturing intangible (or partly each) according to the use of the asset. For example a program (e.g. softwear) used in manufacturing which constitutes a formula, process or know-how (all manufacturing intangibles) and also is a program (a nonmanufacturing intangible) would be treated as a manufacturing intangible; but a program for a marketing campaign, even if also classified as know-how, would be treated as a program and hence as a nonmanufacturing intangible. So too, copyrights may be treated either as manufacturing intangibles or nonmanufacturing intangibles (or as partly each) depending upon the function or the use of the copyright.

Pricing

If the cost sharing payment is made, the island affiliate will be treated as the owner of, and entitled to the full return on, the manufacturing intangibles covered by this election and connected with the product produced, or type of service rendered, in whole or in part, by the island affiliate in the possession. The island affiliate will compute its intercompany price under any of the applicable pricing rules set forth in the section 482 regulations. Use of the resale price method will not be denied merely because the reseller (e.g., the mainland affiliate) added more than an insubstantial amount to the value of the property by the use of intangibles. In such a case, the value of the nonmanufacturing (e.g. marketing) intangibles and any other functions that add value (such as distribution) will be reflected in the resale margin. The use of the resale price method could be denied for other reasons, such as where the return on manufacturing intangibles is minor and no comparables can be found for determining an appropriate mark-up percentage under the resale price method. Thus, a cost plus method may be applied in appropriate cases, after applying the priority-of-application rules of the section 482 regulations, as long as an additional profit amount, representing the return on manufacturing intangibles covered by this election, is permitted the island affiliate. The Internal Revenue Service will not be precluded from applying section 482 with respect to other aspects of the intercompany relationship. The regulations under section 482 and Internal Revenue Service revenue procedures (Revenue Procedure 63-10, as amplified by Revenue Procedure 68-22) will continue to apply except to the extent modified by the election.

Timing of cost sharing payment

If the cost sharing election is made, payment of the required amount must be made by the island affiliate no later than the due date of its tax return for the year (including extensions). To the extent payment is not timely made (e.g., if a greater payment is determined on audit to have been required), the required payment is increased by an amount computed by reference to the interest rate applicable to income tax deficiences. If the failure to make timely payment is due in whole or part to fraud or willful neglect, the island affiliate's election of the cost sharing method is deemed revoked as of the year to which the payment relates.

If a foreign country or possession imposes a tax on the cost sharing payment (or the late payment amount), no foreign tax credit or deduction will be allowed for that tax.

50/50 split of combined taxable income

In general

This election will provide for a split between the island affiliate and its U.S. affiliates of the combined taxable income of the island affiliate and its U.S. affiliates with respect to products produced, in whole or in part, in the possession. 50% of such profit will be allocated to the island affiliate; 50% will be allocated to its U.S. affiliates.

Significant business presence

For an island affiliate to be eligible to apply the profit split, it must satisfy one of the significant business presence tests required for the cost sharing election for the product or type of service covered by the election. In addition, for products produced in whole or part by the island affiliate in the possession, the profit split method is available only if the island affiliate manufactures or produces the product in the possession within the meaning of the controlled foreign corporation provisions of the Code (section 954). If the significant business presence test (including the controlled foreign corporation manufacturing or production rule) is not satisfied for a product or type of service within the product area covered by the election, no intangibles income attributable to that product or type of service will be eligible for the credit.

Combined taxable income

The determination of combined taxable income will be on a product by product basis.

The combined taxable income of the island affiliate and its mainland affiliates from the sale of the product produced in whole or in part in the possession is the excess of the gross receipts from the sale of such product to third parties or foreign affiliates over the total costs relating to such product incurred by the island affiliate and its mainland affiliates. Costs which are treated as relating to a product produced in whole or in part in the possession are all direct and indirect expenses, losses, and other deductions (including marketing expenses) with respect to sales of such product, i.e., the expenses will be "fully-loaded". In this regard, the amount of product area research expenditures properly allocable or apportionable to income from sales of such product may not be less than the amount determined under the cost sharing formula described above. However, if the island affiliate would not be required to cost share under the cost sharing election (e.g. because of the absence of product area research expenditures), the profit split option may still be elected.

Effect of electing 50/50 split

If an election is made, the island affiliate will be entitled to 50 percent of the combined taxable income from the sale of products produced or services rendered in a possession by the island affiliate and sold to third parties or foreign affiliates by the island affiliate or a mainland affiliate. The remainder of the combined taxable income for a product will be allocated to the mainland affiliates. This latter amount may exceed the island affiliate's share of the income from the product if the amount of proportionate product area research expenditures, determined under cost sharing, is in excess of the amount allocable to the combined taxable income absent application of the cost sharing formula. For example, if combined taxable income is $100 without taking into account research and development expenses allocable or apportionable thereto, the amount of such expenses are $10, and the amount computed under cost-sharing (without offsets for island affiliate expenses) is $12, the island affiliate's share of combined taxable income ($100 less $12) is $44 (one-half of $88), and the mainland affiliate's share of combined taxable income is $46 ($100 less $10 of allocable and apportionable expenses and less the island affiliate's $44 share). Thus, the use of this formula is not intended to allow a deduction to any mainland affiliate which would not otherwise be allowable.

Election

An election must be made on or before the due date (including extensions) of the tax return of the electing corporation for its first taxable year beginning after December 31, 1982. An election may be revoked only with the consent of the Secretary. Once revoked, a new election may not be made without the consent of the Secretary. All section 936 affiliates, controlled within the meaning of section 482, producing products or rendering types of services in the same product area will be required to elect the same option for that product area, except that a different method may be used for bona fide export sales from that applicable to other sales.

Transfers of intangibles

Under present law, certain transfers by a U.S. person to a foreign corporation that would otherwise obtain tax-free treatment are taxable unless the Internal Revenue Service issues a ruling that they do not have as one of their principal purposes the avoidance of Federal income tax (sec. 367). The Internal Revenue Service has published guidelines stating when the Service will and will not issue rulings that transactions do not have a tax avoidance purpose. Under the guidelines certain transfers of property for the active conduct of a trade or business abroad are ordinarily not taxable (Rev. Proc. 68-23, 1968-1 C.B. 821 and other releases). However, transfers to foreign corporations of patents, trademarks, and similar intangibles for use in connection with a U.S. trade or business or with manufacturing for sale or consumption in the United States generally are subject to a toll charge under these guidelines.

By negative implication, transfers of intangibles for use purely in connection with a foreign trade or business or manufacturing for sale or consumption outside the United States generally may not be taxable. The conferees recognize that the Internal Revenue Service has authority, under the present law, to find a tax avoidance purpose when an intangible asset is transferred to a foreign corporation. Whether or not the guideline is appropriate as a general rule, the conferees are aware that, as a result of this legislation, some taxpayers have stated that they would remove investment from Puerto Rico and transfer possession-related intangibles to foreign jurisdictions. The conferees believe that such transfers would ordinarily have as one of their principal purposes the avoidance of Federal income tax.

The conference agreement amends the provision of the Code dealing with tax-free transfers to foreign corporations to treat a transfer of a possession-related intangible to a foreign corporation as a transfer pursuant to a plan having as one of its principal purposes the avoidance of Federal income taxes. The provision applies to a transfer by a possession corporation or used as a transfer by an affiliated U.S. corporation where the intangible property was being used (or held for use) by an affiliated possessions corporation. The Secretary may, subject to such terms and conditions as he may impose, allow nonrecognition treatment with respect to such transfers, if the Secretary is satisfied that the transfer will not result in the reduction of current or future Federal income taxes.

The conference agreement also subjects to tax post-July 1, 1982, sales of intangible property to related persons. The income from such sales is U.S. source income, and the cost-sharing and 50/50 profit-split elections do not apply with respect to that income. The income from such sales will not affect the corporation's qualification (under the possessions source and active income tests) as possessions corporation.

Revocation of section 936 election

Under present law, an election of the application of section 936 may be revoked before ten years only with the consent of the Secretary. The conferees anticipate that because of the basic change in the taxation of possessions corporations the Secretary will consent to the revocation of an election by a section 936 corporation provided the election is in effect for the corporation's last taxable year beginning before January 1, 1983. The conferees intend that this liberal consent policy apply only if the consent is requested on or before December 31, 1983, and that the Secretary be permitted to impose conditions on such revocation, such as requiring that the taxpayer obtain the Secretary's consent before reelecting the application of section 936.

8. Tax-Exempt Obligations

a. Restrictions on tax-exempt bonds for private activities

Present law

General rule

Interest on State and local government obligations generally is exempt from Federal income tax; however, industrial development bonds (IDBs) are taxable except when issued for certain specified purposes.

Interest on IDBs is tax-exempt if the bonds are issued to finance the following activities: (1) projects for low-income residential rental property; (2) sports facilities; (3) convention or trade show facilities; (4) airports, docks, wharves, mass commuting facilities, and parking facilities; (5) sewage and solid waste disposal facilities, and facilities for the local furnishing of electricity or gas; (6) air or water pollution control facilities; (7) certain facilities for the furnishing of water; (8) qualified hydroelectric generating facilities; and (9) qualified mass commuting vehicles. In addition, the interest on certain IDBs issued for the purpose of acquiring or developing land as a site for an industrial park is exempt from taxation.

Present law also permits unlimited tax-exempt financing for student loans and organizations that qualify for tax-exemption under section 501(c)(3), such as private, nonprofit hospitals and private, nonprofit educational institutions.

Small-issue exception for IDBs

Present law also permits tax exemption for certain "small issue" IDBs if the proceeds are used for the acquisition, construction, or improvement of land or depreciable property. Unlike the bonds for exempt activities, discussed above, there are no restrictions on the business activities in which land and depreciable property financed with "small issue" IDBs can be used.

This exception applies to issues of $1 million or less without regard to the total capital expenditures for the facility (i.e., the $1 million "clean limit" exception).[1] At the election of the issuer, the limitation may be increased to $10 million where certain capital expenditures are taken into account. In the case of facilities with respect to which an urban development action grant ("UDAG grant") under the Housing and Community Development Act of 1974 has been made, capital expenditures of up to $20 million are allowed.

Both the $1 million and $10 million limitations are determined by aggregating the face amount of all outstanding small issues for all facilities used by the same or related principal users which are located within the same county or same incorporated municipality. In addition, the $10 million limitation is reduced to the extent that the principal users of the facilities incur certain capital expenditures in the same county or same incorporated municipality during the six-year period beginning 3 years before, and ending 3 years after, the issuance of the bonds.

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[1] Before promulgation of Rev. Rul. 81-216, 1981-36 I.R.B. 6 (September 8, 1981), discussed below, small issue IDBs could be marketed as a separate IDB issue in combination with exempt activity IDBs for a single business project.

Other rules

Under present law, facilities financed with tax-exempt IDBs may be depreciated under the Accelerated Cost Recovery System (ACRS) or other available accelerated methods of cost recovery provided under the Code. IDB-financed property also may qualify for the investment tax credit.

Present law is unclear on the length of time that bonds may be outstanding in relation to the economic life of the property financed with tax-exempt financing.

Present law imposes no reporting requirements on issuers of tax-exempt bonds for private activities. Additionally, there are no Federal procedural requirements governing the manner in which such bonds are issued.

House bill

No provision.

Senate amendment

Restrictions on tax-exempt bonds for private activities

Information reporting requirement for all tax-exempt bonds for private activities

The Senate amendment provides that bonds are not tax exempt unless the issuers of all bonds used to finance private activities report certain information (including the amount of the lendable proceeds, the interest rate, term of the issue, and principal users) to the IRS on such bonds issued by them during the preceding calendar quarter. The reporting requirement applies to all IDBs, student loan bonds,[2] and tax-exempt bonds a major portion of the proceeds of which are used by charitable, etc. organizations (described in sec. 501(c)(3)). The required reporting also applies to refunding issues even if the original bonds were issued before 1983, if the refunding occurs after 1982.

This provision is effective for bonds, including refunding issues, issued after December 31, 1982.

Public approval requirements for all IDBs

The Senate amendment establishes new approval requirements for issuers of IDBs.[3] Failure to comply with these requirements will result in loss of tax exemption for the interest on the bonds. The new requirements are twofold: (1) reasonable notice must be given and a public hearing held and (2) issuance of the bonds must be approved after the hearing by an elected public official or elected legislative body. Alternatively, a voter referendum on a particular project or bond issue, held at such time and in such manner as referenda on other issues affecting government spending under applicable State and local law, may be used in place of the public hearing and elected representative approval requirements.

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[2] Student loan bonds include State or local government bonds used to finance, directly or indirectly, loans for educational or related expenses regardless of whether the bonds or educational loans are guaranteed by the Federal or State governments.

[3] This restriction applies only to IDBs; therefore, it generally does not apply to student loan bonds or bonds for tax-exempt organizations described in section 501(c)(3) (other than bond proceeds used in an unrelated trade or business of the organization).

The public approval requirements are effective for obligations, including refunding issues, issued after December 31, 1982. The public approval requirements do not apply, however, to (1) issues solely to refund a prior issue, which was issued in compliance with the requirements, where the maturity of the bonds is not extended and (2) certain issues of a governmental unit for a facility issued within a 7-year period pursuant to a plan of financing where the proceeds from all obligations issued under that plan are used to finance the facilities of the principal users described in that plan.

Restriction on cost recovery deductions for certain property financed with IDBs

The Senate amendment provides that property that is placed in service after December 31, 1982, generally is allowed cost recovery deductions at a slower rate than those allowed under ACRS or other accelerated cost recovery provisions of the Code, to the extent that the facilities are financed by an IDB. In lieu of deductions under ACRS, the cost of property financed with IDBs must be recovered using the straight-line method over the ACRS life for the property involved. This limitation applies to both the first owner of the property and to any subsequent owners who acquire the property while the IDBs (including any refunding issues) are outstanding.

The amendment includes several exceptions permitting the cost of certain types of facilities financed in whole or in part with IDBs to continue to be recovered under ACRS: low income rental housing, municipal sewage and solid waste disposal facilities, air or water pollution control facilities used in connection with a plant or other property in operation before July 1, 1982, and facilities for which a UDAG grant equalling or exceeding 5 percent of the total capital expenditures on the facility is made.

The amendment also includes transition rules permitting the cost of certain property placed in service after 1982 to be recovered under ACRS if (1) a binding contract existed on July 1, 1982, and at all times thereafter, committing the purchaser to incur significant expenditures; (2) construction began before July 1, 1982; or (3) the bonds with which the property is financed were issued before July 1, 1982.

Restrictions on "small issue" IDBs

Sunset of small issue exception.—The Senate amendment repeals the small issue exception with respect to obligations (including refunding issues) issued after September 30, 1987.

Restriction on "clean limit" small issue exception.—The Senate amendment provides that, effective after the date of enactment, the $1 million "clean limit" small issue exception (sec. 103(b)(6)(A)) is not available for any IDBs issued as part of a single issue with any other obligations, the interest on which is tax-exempt under any provision other than the small issue exception.

Elimination of small issue exception to finance certain facilities.—The Senate amendment eliminates the small issue exception for bonds issued after December 31, 1982, if—

(i) more than 25 percent of the proceeds of the issue are used to provide a facility the primary purpose of which is automobile sales or service or the provision of recreation or entertainment; or

(ii) any portion of the proceeds of the issue is to be used to provide the following: any private or commercial golf course, country club, massage parlor, tennis club, skating facility (including roller skating, skateboard, and ice skating), racquet sports facility (including handball and racquetball courts), hot tub facility, suntan facility, or racetrack.

Conference agreement

The conference agreement follows the Senate amendment with several modifications.

Public hearing and approval requirements for all IDBs

The conferees intend to clarify the application of the rule requiring a public hearing and approval by an elected official or legislative body in order to issue IDBs. Under the conference agreement, public hearings and approval by an elected official or legislative body are required by both the issuing jurisdiction and the jurisdiction where the facilities are located.

Where the facilities are located entirely within the geographic jurisdiction of the issuing governmental unit, only one public hearing and approval are required even though the facilities may be located in several different subdivisons of the issuing governmental unit.

Where facilities are not located within the geographic jurisdiction of the issuing governmental unit at least one governmental unit having geographic jurisdiction over each facility must hold a hearing and approve the bond issue. This may be either a single governmental unit or a series of smaller governmental units that may be subdivisions of the single governmental unit. For example, where a governor of a state is to approve the issuance of bonds for facilities located in that state (even though located in several counties), only the state is required to have a public hearing on that bond issue. Where, however, a facility is located in several counties and each county's elected executive officer is to approve the issuance of the bonds for facilities located in that county, each county is required to have a public hearing on that bond issue.

Where the facility is located in more than one state, then the hearing and approval requirements are applied as if there were separate facilities in each state. Thus, for example, in the case of electric transmission lines that cross state lines, the transmission lines located in each state are treated as separate facilities and each state or its counties where the separate facilities are located is required to meet the public hearing and approval requirements.

The conferees intend that the hearing may be held directly by the governmental unit or its agencies or by a person who issues bonds on behalf of that governmental unit. Generally, the conferees intend that the hearing be held at times and in places that would be convenient for persons affected by the facilities financed by the IDBs. However, where an IDB will finance more than one facility at different locations, it is not necessary that separate hearings be held for each facility. For example, where a state agency proposes to issue an IDB to finance projects throughout the state, only one hearing need be held somewhere within the state for all the facilities financed with the IDB provided adequate public notice of the hearing is given in all areas where facilities are to be located.

In addition, the conferees intend to clarify that the special rule which permits approval of a plan of financing for up to 3 years also applies to refunding obligations issued within that 3-year period. For example, the rule covering plans of financing would cover situations where IDBs are issued and then refunded one or more times within the 3-year period. The 3-year period commences on the date that obligations are first issued pursuant to the approval of the plan.

Restrictions on cost recovery deductions for certain property financed with IDBs

Under the conference agreement, the effective date for the restrictions on cost recovery deductions is clarified to provide that certain multi-family rental projects are exempt from the cost recovery provisions of the bill when the project was exempt from restrictions on the use of IDBs for multi-family housing under the Mortgage Subsidy Bond Tax Act of 1980.

With regard to the exemption from the restrictions of the bill for sewage and solid waste disposal facilities, the conferees wish to clarify that facilities will qualify for this exception regardless of whether the solid waste or sewage is collected from an area within part or all of a government unit or an area larger than one governmental unit; regardless of whether the facilities are operated by a governmental unit or a private company; and regardless of whether the facilities accept for processing all types of waste (as long as the waste accepted is collected from the general public). Solid waste need not include source separated or recyclable materials.

For this purpose, the general public includes commercial and other businesses but only if the solid waste collected from businesses is collected from them in their capacities as members of the general public and not as members of a limited group (such as groups that have special types of waste not processable by normal waste facilities serving the general public).

The effective date for the cost recovery rule provides that the new limitations do not apply to property where construction on the property began before July 1, 1982, as long as the original use of the property began with the taxpayer. The conferees intend that all property which is a part of the facilities described in the inducement resolution adopted before July 1, 1982, pursuant to which the bonds are issued, is treated as under construction where any part of those facilities is under construction before July 1, 1982. Moreover, the conferees intend that all such property is under the transitional rule even though part of the facilities are transferred by the taxpayer prior to their being placed in service and even though properties which are part of the facilities are placed in service before the completion of construction of other properties which are part of those facilities.

Sunset of small issue exception

The conference agreement modifies the Senate amendment by providing that the small issue exemption will not apply with respect to obligations issued after December 31, 1986.

Elimination of small issue exception to finance certain facilities

The conference agreement modifies the rule of the Senate amendment which restricts the use of small issue IDBs where 25 percent of the bond proceeds are used for certain purposes to include in the list of prohibited purposes the providing of retail food and beverage services. For this purpose, retail food and beverage services includes eating and drinking places, but does not include grocery stores.

Relationship of bond maturity to life of assets

The conference agreement provides a rule that limits the average length of the maturity of all industrial development bonds (IDBs). Under the rule, the weighted average maturity [4] of all obligations of an issue cannot exceed the weighted average estimated economic life [5] of the assets financed with the proceeds of the issue [6] by more than 20 percent. The economic life of an asset is to be measured from the later of the date the bonds are issued or the date the assets are reasonably expected to be placed in service. For example, if the proceeds of the bond are used to purchase assets with an average estimated economic life of 10 years, the maximum average maturity for the bonds may not exceed 12 years from the date the assets are expected to be placed in service where the bonds are issued after that date.

In general, the economic life of assets is to be determined on a case-by-case basis. However, in order to provide guidance and certainty, the conferees intend that the administrative guidelines established for the useful lives used for depreciation prior to the ACRS system (i.e., the midpoint lives under the ADR system where applicable and the guideline lives under Rev. Proc. 62-21, 1962-2 C.B. 418, in the case of structures) may be used to establish the economic lives of assets. However, the taxpayer can issue bonds with maturities longer than these administrative guidelines would allow where the taxpayer can show, on the basis of the facts and circumstances, that the economic life to the principal user or users of the assets for whom the bonds are issued is longer than the lives established by the administrative guidelines.

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[4] The weighted average maturity of obligations of an issue is determined by taking into account the issue price (as defined in sec.1232) of each obligation.

[5] The weighted average estimated useful life of assets financed with the proceeds of an issue is determined by taking into account the cost of each asset financed with the proceeds of the issue.

[6] Where the amount of the bond is less than the cost of the facilities, the assets financed with the bond shall include an allocable portion of the facilities which may be purchased by the bond proceeds under the bond indenture.

The conference agreement provides special rules for the treatment of land in determining the weighted economic life of the assets financed by the bonds. Where less than 25 percent of the bond proceeds are used to acquire land, the economic life of the assets financed by the bonds is determined without regard to the land (i.e., the maximum maturity of the bonds is based on the economic life of the assets financed by the bonds other than land). Where 25 percent or more of the bond proceeds are used to acquire land, then the economic life of the assets acquired by the bonds will be determined by assuming that the land has a life of 50 years.

b. Other amendments affecting industrial development bonds

Present law

General rule

Interest on State and local government obligations generally is exempt from Federal income tax; however, industrial development bonds (IDBs) are taxable except when issued for certain specified purposes.

Interest on IDBs is tax-exempt if the bonds are issued to finance the following activities: (1) projects for low-income residential rental property;[1] (2) sports facilities; (3) convention or trade show facilities; (4) airports, docks, wharves, mass commuting facilities, and parking facilities; (5) sewage and solid waste disposal facilities, and facilities for the local furnishing of electricity or gas;[2] (6) air or water pollution control facilities;[3] (7) certain facilities for the furnishing of water; (8) qualified hydroelectric generating facilities; and (9) qualified mass commuting vehicles. In addition, the interest on certain IDBs issued for the purpose of acquiring or developing land as a site for an industrial park is exempt from taxation.

Small-issue exception for IDBs

Present law also permits tax exemption for certain "small issue" IDBs if the proceeds are used for the acquisition, construction, or improvement of land or depreciable property. Unlike the bonds for exempt activities, discussed above, there are no restrictions on the business activities in which land and depreciable property financed with "small issue" IDBs can be used.

This exception applies to issues of $1 million or less without regard to the total capital expenditures for the facility (i.e., the $1 million "clean limit" exception).[4] At the election of the issuer, the limitation may be increased to $10 million, where certain capital expenditures are taken into account. In the case of facilities with respect to which an urban development action grant ("UDAG grant") under the Housing and Community Development Act of 1974 has been made, capital expenditures of up to $20 million are allowed.

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[1] IDBs used to finance low-income residential rental property are tax-exempt only if the obligations are issued in registered form and if 20 percent or more (15 percent or more in the case of targeted area projects) of the units in each project are occupied by individuals of low or moderate income. The term low or moderate income is defined by reference to the meaning of that term under section 8 of the United States Housing Act of 1937. The 20 percent requirement (15 percent in targeted areas) must be met for 20 years with respect to any obligations issued before January 1, 1984.

[2] Under present law, a facility for the local furnishing of electricity is defined as a facility whose service area does not exceed two counties or a city and one contiguous county. A facility for the local furnishing of gas is defined as a facility whose service area does not exceed two counties. Present law does not permit issuance of IDBs to finance facilities for local district heating or cooling.

[3] Present law generally prohibits the issuance of IDBs to acquire existing facilities if a substantial user of the facilities prior to the acquisition will be a substantial user after the acquisition.

[4] Before promulgation of Rev. Rul. 81-216, 1981-36 I.R.B. 6 (September 8, 1981), discussed below, small issue IDBs could be marketed as a separate IDB issue in combination with exempt activity IDBs for a single business project.

Both the $1 million and $10 million limitations are determined by aggregating the face amount of all outstanding small issues for all facilities used by the same or related principal users which are located within the same county or same incorporated municipality. In addition, the $10 million limitation is reduced to the extent that the principal users of the facilities incur certain capital expenditures in the same county or same incorporated municipality during the six-year period beginning 3 years before, and ending 3 years after, the issuance of the bonds.[5]

Other rules on IDBs

In Rev. Rul. 81-216,[6] the Internal Revenue Service held that lots of bonds are a single issue if the bonds are sold (1) at substantially the same time, (2) pursuant to a common plan of marketing, (3) at substantially the same interest rate, and (4) with a common or pooled security. On October 8, 1981, the IRS proposed regulations that provided essentially the same rules as Rev. Rul. 81-216 and proposed to revoke that revenue ruling.[7]

Under present law, advance refundings of industrial development bonds (IDBs) generally are prohibited. However, advance refunding is permitted for IDBs for certain convention and trade show facilities, airports, docks, wharves, and mass commuting facilities (Code sec. 103(b)(7)).

House bill

No provision.

Senate amendment

Exclusion of research and development expenditures from capital expenditure limitation

The Senate amendment excludes research wages and supplies (of a type for which a credit may be available under section 44F) from the capital expenditures that are to be taken into account under the $10 million limitation for small issue bonds. This provision is effective for research expenditures made after the date of enactment.

Local furnishing of gas

The Senate amendment provides that local furnishing of gas from a facility includes the furnishing solely within an area comprised of a city and one contiguous county. Thus, under the amendment, tax-exempt financing is made available in the case of a facility for the furnishing of gas (which otherwise meets the requirements of sec. 103) provided that the service area of the facility comprises no more than two contiguous counties or a city and one contiguous county. This provision is effective for bonds issued after the date of enactment.

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[5] Certain research and development expenditures are treated as capital expenditures for purposes of the $10 million limitation whether or not the taxpayer elects to deduct currently such expenditures under Code section 174.

[6] 1981-36 I.R.B. 6 (September 8, 1981).

[7] 46 Fed. Reg. 50014 (October 8, 1981).

Local district heating and cooling facilities

The Senate amendment exempts from tax interest on IDBs issued after the date of enactment to finance local district heating or cooling facilities. A local district heating or cooling facility includes equipment and other property used as an integral part of a local heating or cooling system, but does not include facilities which produce the hot water, chilled water, or steam, or facilities that are owned for tax purposes by the consumer. A heating or cooling system is considered local if it has a service area comprised of no more than two contiguous counties or a city and one contiguous county.

Multiple lot IDBs

The Senate amendment provides that, for bonds issued after the date of enactment, separate lots of obligations will be treated as part of the same issue only if the proceeds of the obligations are to be used to finance facilities which are located in more than one State or have the same person or related persons as its principal user or principal users. For this purpose, a principal user includes a person (other than a governmental unit) that guarantees directly or indirectly the repayment of the obligations or that aids in arranging issuance of the obligations, and that person provides property[8] or a franchise or trademark to be used in connection with the facilities financed with the obligations.

Regional pollution control authorities

The Senate amendment permits tax-exempt IDBs to be issued for use by a regional pollution control authority to acquire existing air or water pollution control facilities which the authority itself will operate under certain conditions. This provision applies to expenditures made after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment with three modifications.

Advance refunding of certain IDBs of the Port Authority of St. Paul

The conference agreement provides that certain IDBs of the Port Authority of St. Paul, Minnesota may be advance refunded as long as the refunded obligations are retired within six months after any call premium on the refunded bonds lapses.

Multiple lot IDBs

The conferees wish to clarify that lots of obligations which are not treated as a single issue pursuant to the transitional rules adopted by the Internal Revenue Service for the rule provided in Rev. Rul. 81-216 are not considered as a single issue and thus are not subject to the rules of the conference agreement on multiple lot IDBs.

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[8] For this purpose, property does not include a letter of credit.

IDBs for multi-family residential rental projects

The conference agreement makes two changes in the rules for IDBs used to finance residential rental property for low and moderate income families. First, the conference agreement provides a separate definition of individuals of low and moderate income by adopting the definition of that term under the section 8 program except that the applicable percentage will be 80 percent of the area median income (regardless of the percentage used under the section 8 program).

Second, the duration of the requirement that 20 percent of the housing units in a project be occupied by individuals of low or moderate income (15 percent in targeted areas) is also changed. Under the conference agreement, that rule applies from the date the project is first occupied and continues until the later of (1) 10 years after over one-half of the project is first occupied, (2) a date ending when 50 percent of the maturity of the bonds having the longest maturity has expired, or (3) the date on which any section 8 (or comparable) assistance terminates. As under present law, all of the units of the project financed with tax-exempt IDBs must remain as rental units for the length of the targeting requirement.

The changes to the requirements for IDBs for low and moderate income residential rental property apply to obligations issued after the date of enactment other than obligations which are exempt from the restrictions of the Mortgage Subsidy Bond Tax Act of 1980.

c. Amendments to Mortgage Subsidy Bond Tax Act

Present law

The Mortgage Subsidy Bond Tax Act of 1980 established rules directing the subsidy from the use of tax-exempt bonds for housing. Under the Act, all of the mortgages financed from tax-exempt bond proceeds must be provided to mortgagors, each of whom did not have a present ownership interest in a principal residence at any time during the three prior years (i.e., the first-time home purchaser limitation). All of the mortgages (or other financing) provided from the bond proceeds, except qualified home improvement loans, must be used to purchase residences whose purchase price does not exceed 90 percent (110 percent in targeted areas) of the average area purchase price.

In order to be a qualified mortgage issue, the issue must meet certain requirements regarding arbitrage as to both mortgage loans and nonmortgage investments. First, the effective rate of interest on mortgages provided under the issue cannot exceed the yield on the issue by more than one (1.0) percentage point. Second, the reserve for future debt service established in connection with the bonds must be reduced as future annual debt service is reduced. The maximum amount that can be invested as unrestricted yield in nonmortgage investments is 150 percent of the debt service on the issue for the bond year, and arbitrage earned by the issuer on nonmortgage investments must be paid or credited to the mortgagors or paid to the Federal Government.

There are no provisions that relate specifically to the treatment of cooperative housing corporations under these rules.

House bill

No provision

Senate amendment

The Senate amendment changes four of the requirements for qualified mortgage bonds:

First-time home purchaser limitation.—The Senate amendment provides that 80 percent of the lendable proceeds of a mortgage subsidy bond must be made available to first-time home purchasers.

Purchase price limitations.—The Senate amendment increases the purchase price limitation to 110 percent (120 percent in a targeted area) of the average area purchase price.

Arbitrage limitations.—The 1.0-percentage points limit is replaced by a limit which varies with the size of the issue, beginning at $1\frac{1}{8}$ percentage points for smaller issues and decreasing to $1\frac{1}{16}$ percentage points for issues of $100 million or larger.

Reserve liquidations.—The rule requiring reserve liquidations does not apply to the extent it requires disposition of any nonmortgage investment resulting in a loss in excess of the amount of undistributed arbitrage profits on such investments.

Conference agreement

The conference agreement follows the Senate amendment with the following modifications:

First-time home purchaser limitation

The first-time home purchaser rules will require that 90 percent of the lendable proceeds of a mortgage subsidy bond go to first-time home purchasers.

Arbitrage

The effective rate of interest on mortgages financed with tax-exempt bonds may not exceed the yield on the issue by more than 1⅛ (1.125) percentage points. The conference agreement clarifies that, in determining the effect of prepayments of mortgage principal on the computation of the effective rate of mortgage interest, prepayments of principal shall be treated as received on the last day of the month in which the issuer reasonably expects to receive such prepayments.

Cooperative housing

In the case of any cooperative housing corporation (as defined in Code sec. 216), each dwelling unit shall be treated as if it were actually owned by the person entitled to occupy that unit by reason of his or her ownership in the cooperative housing corporation. In addition, any indebtedness of the corporation that is allocable to the dwelling unit shall be treated as if it were indebtedness of the shareholder who is entitled to occupy the dwelling unit.

The conference agreement provides that any issue that provides financing to a cooperative housing corporation that is not located in a targeted area may be combined with one or more other issues which in sum satisfy the present law requirement that at least 20 percent of the proceeds of the issues will be devoted to owner-financing of residences in targeted areas for a period of at least one year.

The conferees also intend that, in applying the rules of section 103A to cooperative housing corporations, the acquisition cost for a cooperative unit is to be defined to include a proportionate share of the underlying blanket mortgage plus the purchase price of the shares.

In addition, loans to cooperative housing corporations for rehabilitation may qualify for tax-exempt financing under section 103A(1)(7) to the same extent as if each shareholder receives a proportionate share of the loan. In the case of tax-exempt financing used for the construction of a residential building owned by a cooperative housing corporation, unlimited arbitrage otherwise allowed during a 3-year temporary period would be permitted for only one year.

Finally, the conferees intend to clarify that tax-exempt financing may be allowable under section 103(b)(4)(A) where a cooperative leases property from another person and the shareholders of the cooperative meet the targeting provisions of that section.

9. Mergers and Acquisitions

a. Partial liquidations

Present law

A distribution in redemption of a corporation's stock pursuant to a plan is a partial liquidation if it is one of a series of distributions in redemption of all the stock or it is not essentially equivalent to a dividend and occurs within the taxable year in which the plan is adopted or the succeeding year (sec. 346(a)).

In determining that a distribution is not essentially equivalent to a dividend in applying the tests for a partial liquidation, generally a contraction of the corporation's business is required. A distribution may constitute a partial liquidation even though it is made pro rata among the corporation's shareholders.

If the distribution consists of the assets of, or is attributable to the corporation's ceasing to conduct, a trade or business conducted for 5 years or more before the distribution and was not, within the 5-year period, acquired by the corporation in a taxable transaction and the corporation, after the distribution, continues to conduct another trade or business with a similar history, the distribution is treated as a partial liquidation (sec. 346(b)).

No gain or loss to the distributing corporation is recognized on a distribution in a partial liquidation (sec. 336(a)). Exceptions are provided for disposition of installment obligations and distributions of LIFO inventory. In addition, the various recapture rules of present law override sec. 336. If, however, the corporation, rather than distributing assets, sells the assets and distributes the proceeds to its shareholders in a partial liquidation, gain or loss is recognized to the corporation on the sale.

Shareholders receiving a distribution in partial liquidation are treated as receiving the amount distributed in exchange for their stock and, if the stock redeemed in the transaction is a capital asset to the shareholder, capital gain or loss results from the transaction. The basis of any assets received in a partial liquidation is their fair market value at the time of the distribution.

House bill

No provision.

Senate amendment

The Senate amendment modifies the treatment of partial liquidations. Only noncorporate shareholders are treated as receiving the amount distributed in exchange for their stock. Distributions to corporate shareholders are governed by the provisions of present law other than those relating to partial liquidations.

Under the Senate amendment, gain to the distributing corporation is recognized, with an exception, when appreciated property is distributed in partial liquidation to noncorporate shareholders. The exception applies to distributions made with respect to qualified stock. Qualified stock is stock that has been held by certain noncorporate shareholders for the 5-year period ending on the date of distribution or (if less) for the period the corporation has been in existence. The shareholder must have held at least 10 percent in value of the distributing corporation's stock throughout such period. The constructive ownership rules of section 318 apply in determining ownership. In applying the attribution rules of section 318(a)(1), the group of persons among whom ownership is attributed is expanded to include individuals described in section 267(c)(4) and the spouses of such individuals.

Under this rule, it is not required that the stock redeemed be held by the shareholder for five-years. It is sufficient that the shareholder hold (or be treated as holding) 10 percent of the stock throughout the five year period.

The Senate amendment authorizes the Secretary of the Treasury to prescribe regulations, where necessary, to ensure that revision of the treatment of partial liquidations will not be circumvented through the use of other provisions of present law or regulations, including the consolidated return regulations. The Senate amendments apply generally to distributions after August 31, 1982. However, present law continues to apply to distributions with respect to which, on July 22, 1982, there was a ruling request pending with the Internal Revenue Service as to whether such distributions qualify as a partial liquidation (or a ruling was granted within one year prior to July 12, 1982 that the distributions qualified as a partial liquidation) and the distributions are pursuant to a plan of partial liquidation adopted by the Board of Directors before September 1, 1982 (or, if later, within 90 days after the ruling was granted). Present law applies as well to distributions pursuant to a plan of partial liquidation adopted before July 1, 1982; distributions pursuant to a plan of partial liquidation adopted before October 1, 1982, where control (as defined in sec. 368(c)) is acquired between December 31, 1980, and July 1, 1982, and conduct of the business is conditioned on approval by a State regulatory agency; distributions pursuant to a plan of partial liquidation adopted within 90 days after the acquisition is approved by a Federal regulatory agency where control is acquired after July 1, 1982, pursuant to a binding contract outstanding on December 31, 1980; and distributions pursuant to a plan of liquidation adopted by October 1, 1982, where control was acquired between December 31, 1981, and July 1, 1982.

Conference agreement

General rules

The conference agreement follows the Senate amendments with technical modifications. The conference agreement adds a new section 302(b)(4) under which distributions in redemption of a noncorporate shareholder's stock are treated as payments in exchange for the stock under section 302(a) if such distributions are in partial liquidation of the distributing corporation. For this purpose, a partial liquidation is defined in new section 302(e) which continues the definition of a partial liquidation in present law section 346(a)(2) and section 346(b) which are repealed by the bill. As under present law section 346(a)(2), the determination that a distribution is not essentially equivalent to a dividend for purposes of satisfying the partial liquidation definition is to be made with reference to the effect of the transaction on the distributing corporation and not with reference to its effect at the shareholder level. This is made an explicit statutory test under the conference agreement.

Under present law, a distribution in partial liquidation may take place without an actual surrender of stock by the shareholders (*Fowler Hosiery Co.* v. *Commissioner),* 301 F.2d 394 (7th Cir. 1962). A constructive redemption of stock is deemed to occur in such transactions (Rev. Rul. 81-3, 1981-1 C.B. 125). The conferees intend that the treatment of partial liquidations under present law section 346(a)(2) and (b) is to continue for such transactions under new section 302(e). Recognition of gain to the distributing corporation under section 311(d) as amended by the bill will not require an actual surrender of stock by the shareholders, if the distribution qualifies as a partial liquidation under new section 302(e) without an actual surrender of stock.

Whether or not a redemption is treated as a distribution in partial liquidation is determined without regard to whether or not the redemption is pro rata with respect to all the shareholders of the corporation. A distribution in partial liquidation, pursuant to section 302(b)(4), will be treated as a distribution in exchange for stock under section 302(a) without regard to whether the redemption satisfies the requirements of paragraphs (1), (2), or (3) of section 302(b). A distribution in partial liquidation that also terminates a shareholder's interest in the corporation will be treated as a distribution in exchange for stock under section 302(a) without regard to section 302(c)(2).

The conference agreement modifies the definition of qualified stock by providing that the period a distributing corporation has been in existence includes the period of existence of a predecessor corporation and the 10-percent stock ownership requirement must be satisfied with respect to the period of existence of both the distributing and predecessor corporations.

For purposes of determining whether stock is held by a shareholder who is not a corporation in applying new section 302(b)(4), stock held by a partnership, estate, or trust will be treated as if it were actually held proportionately by its partners or beneficiaries.

As under present law, distributions in partial liquidation that are treated under section 302(a) as distributions in exchange for stock pursuant to new section 302(b)(4) will be subject to the collapsible corporation rules of section 341.

Distributions in partial liquidation after August 31, 1982, are subject to the new rules for such distributions provided by the conference amendment.

Effective dates

Distributions in partial liquidation after August 31, 1982, except as otherwise provided, are subject to the new rules for such distributions provided by the conference agreement. The conference agreement makes several modifications to the exceptions provided in the Senate amendment.

The exception for rulings granted by the Internal Revenue Service as to partial liquidation treatment is modified to include rulings granted within the period beginning on July 12, 1981, and ending on July 22, 1982, and the date before which the plan of partial liquidation must be adopted, for both ruling requests pending on July 22, 1982, or rulings granted, is October 1, 1982 (or 90 days after the ruling was granted, if later). A request will be treated as pending on July 23, 1982, and thereafter notwithstanding that, pursuant to negotiations with the Internal Revenue Service, a revision or modification of the request is filed or additional information is submitted.

The exception for plans of partial liquidation adopted before July 1, 1982, is extended to include plans adopted before July 23, 1982.

The exception for acquisitions of control during 1982 and before July 1, 1982, is expanded to include acquisitions of control before July 23, 1982. Control is acquired after July 22, 1982, for purposes of this rule even if an amount of stock constituting less than control was held on such date. In addition, an exception applies if, during March and April 1982, one-third or more of the shares of a corporation were acquired and the intention to acquire control is evidenced by documents filed with the Federal Trade Commission and if control is thereafter acquired. For either exception to apply, a plan of partial liquidation must be adopted by October 1, 1982.

Under the conference agreement, an exception is provided for acquisitions of control after July 22, 1982, pursuant to a tender offer or binding contract outstanding on such date. The plan of partial liquidation must be adopted before the later of October 1, 1982, or, if the acquisition is subject to approval by a Federal regulatory agency, the date which is 90 days after the date on which such approval becomes final in accordance with law. A public announcement of an intention to acquire control pursuant to a tender offer will be treated as a tender offer for purposes of this exception if the proposal is subject to intervention by a foreign regulatory body before which the proposal is pending on July 22, 1982, and the plan of partial liquidation is adopted within 90 days after the date on which the foreign regulatory body approves of the offer.

The exception applicable under the Senate amendment where control was acquired after December 31, 1980, is limited to acquisitions of insurance companies where the conduct of the insurance business by the distributee corporation is conditioned on approval by one or more State regulatory authorities. This exception applies if control was acquired either by the distributee corporation or its parent. The period within which control must be acquired is extended to cover acquisitions before July 23, 1982, and, as under the Senate amendment, a plan of partial liquidation must be adopted before October 1, 1982.

For purposes of these exceptions, a plan of partial liquidation is treated as adopted on the date on which it is approved by the corporation's Board of Directors. Such date is also to be treated as the date of adoption of a plan for purposes of determining the period within which distributions under the plan must be made in applying section 346(a)(2) (as in effect before its repeal by the amendments made by the bill).

A contract will be treated as a binding contract for purposes of applying the exceptions if it is binding on the acquiring corporation and even though it is subject to approval by a vote of the shareholders, the obtaining of financing to consummate the acquisition and other similar conditions.

Property acquired in distributions to which these exceptions apply will be treated as property acquired before September 1, 1982, in applying the rules of new section 338 requiring consistency of treatment for acquisitions of stock and assets in certain cases.

b. Certain distributions of appreciated property

Present law

When a corporation in a nonliquidating distribution distributes property, the value of which exceeds its basis, in redemption of a portion of the corporation's stock, gain is recognized as though the property were sold (sec. 311(d)(1)). Present law excepts several types of transactions from this requirement.

Exceptions are provided for (1) distributions that terminate the interest of a shareholder who has held at least 10 percent of the corporation's stock for a 12-month period; (2) distributions that consist of stock or obligations in a subsidiary conducting a trade or business that was at least 50 percent owned by the distributing corporation at any time within the preceding 9 years; (3) distributions that consist of stock or securities distributed pursuant to certain anti-trust decrees; (4) distributions to which section 303(a) (relating to distributions in redemptions of stock to pay death taxes) applies; (5) certain distributions to private foundations; (6) certain distributions by regulated investment companies; and (7) certain distributions pursuant to the Bank Holding Company Act.

Notwithstanding these exceptions, present law may permit a transaction that is in form a stock redemption to be treated as a direct sale of assets where the stock ownership is transitory (see Rev. Rul. 80-221, 1980-2 C.B. p. 107).

House bill

No provision.

Senate amendment

The Senate amendment repeals the exceptions in section 311(d)(2) for distributions terminating the interest of a shareholder who has held 10 percent or more of the corporation's stock for one year, for distributions pursuant to antitrust decrees, for distributions pursuant to the Bank Holding Company Act, and modifies the exception for distributions of stock or obligations of a subsidiary.

The bill is not intended to affect the treatment under present law of distributions that are in substance the purchase of assets.

The Senate amendment revises subparagraphs (A), (B), and (C) of section 311(d)(2) to conform the treatment of the distributing corporation to the new rules applicable to partial liquidations and to provide for nonrecognition of gain when stock or obligations of a subsidiary are distributed in redemption of stock in certain transactions analogous to a partial liquidation.

New section 311(d)(2)(A) provides that gain will not be recognized to a corporation distributing property to a corporate shareholder unless section 302(a) applies to the distribution. Distributions in partial liquidation to a corporate shareholder under the Senate amendment generally will be treated similarly to distributions which are not in redemption of stock unless they are non-pro rata distributions to which section 302(b) (1), (2), or (3) applies. Such distributions generally will be treated as dividends or other distributions to which section 301 applies. Gain is not recognized to a distributing corporation on section 301 distributions that are not in redemption of stock and the revised section 311(d)(2)(A) conforms the treatment of the distributing corporation to the treatment of a corporate shareholder on partial liquidation distributions whether or not there is an actual surrender of stock in the transaction.

New section 311(d)(2)(B), relating to distributions of stock or obligations of a corporation, continues the provisions of present law section 311(d)(2)(B) with an amendment requiring at least 50 percent in value of the outstanding stock of the corporation to be distributed with respect to qualified stock (in lieu of the present law requirement that the distributing corporation must have owned at least 50 percent of the corporation's stock within the 9-year period prior to the year of distribution). The Senate amendment further limits the exception to distributions with respect to qualified stock and adds an additional limitation pursuant to which the exception applies only if the distribution would qualify as a partial liquidation under new section 302(e) if the assets, rather than stock or obligations of the corporation, were distributed in the transaction. For purposes of the latter test, such assets will be treated as having been held directly by the distributing corporation throughout the period during which the distributing corporation held at least 50 percent in value of the stock of the corporation whose stock is distributed in the transaction.

New section 311(d)(2)(C) provides the exception pursuant to which gain is not recognized to the distributing corporation on partial liquidation distributions under new section 302(e) that are made with respect to qualified stock.

The amendments relating to distributions of appreciated property in redemption of stock apply to distributions made after August 31, 1982. Of course, the present law provisions of section 336 providing for nonrecognition of gain or loss to the distributing corporation on distributions in partial liquidation will apply to distributions after August 31, 1982, to which, under the effective date provisions in section 226(f) of the bill, the present law partial liquidation provisions apply.

Conference agreement

General rules

The conference agreement generally follows the Senate amendment, with certain technical modifications.

New section 311(d)(2)(A) is redrafted to provide for nonrecognition of gain to the distributing corporation in any case where the basis of property distributed to a corporate shareholder is determined under section 301(d)(2). This rule provides substantially the same nonrecognition rule for property distributions as would the Senate amendment.

Section 311(d)(2)(B) is conformed by the conference agreement to provide for nonrecognition of gain to the distributing corporation on distributions in partial liquidation to which new section 302(b)(4) applies which are made with respect to qualified stock.

Section 311(d)(2)(C) as revised by the conference agreement provides the exception to gain recognition for distributions of stock or obligations of a corporation (hereinafter called the controlled corporation).

For the exception with respect to distributions of stock or obligations of a controlled corporation to apply, as under the Senate amendment, the distribution must be made with respect to qualified stock and more than 50 percent in value of the controlled corporation's stock must be distributed with respect to qualified stock. The conference agreement further requires that substantially all the assets of the controlled corporation consist of the assets of one or more qualified businesses and that no substantial part of the controlled corporation's nonbusiness assets were acquired from the distributing corporation in a transaction to which section 351 applied or as a contribution to capital within the 5 years ending on the date of distribution.

A qualified business is one that was actively conducted throughout the 5-year period ending on the date of distribution and was not acquired within such period by any person in a transaction in which gain or loss was recognized in whole or in part. Section 355, relating to distributions of stock or securities of a controlled corporation, contains a similar active business requirement.

Nonbusiness assets are defined to include any asset not used in the active conduct of a trade or business. For this purpose, cash and other items that provide working capital needs of an active business will be treated as assets used in the active conduct of the business.

Effective dates

Under the Senate amendment, the repeal of present law section 311(d)(2) exceptions is effective for distributions made after August 31, 1982. The conference agreement retains this general effective date but retains the exceptions in sections 311(d)(2)(A) and 311(d)(2)(C) of present law for certain distributions made on or after September 1, 1982. Under the conference agreement, section 311(d)(2)(A) of present law will continue to be applicable to distributions made within 90 days after a ruling is granted under a request pending before the Internal Revenue Service on July 22, 1982, with respect to the application of section 311(d)(2)(A) to a proposed distribution. Also, present law section 31(d)(2)(A) continues to apply to distributions, otherwise qualifying for such treatment, which are made on or before August 31, 1983, with respect to stock acquired after 1980 and before May 1982.

Finally, the redemption of preferred and common stock by a forest products company pursuant to a binding contract in effect on August 31, 1982, and at all times thereafter, where all distributions must be pursuant to one of the two options set forth in the contract will continue to be subject to present section 311(d)(2)(A) to the extent timberland is distributed to the shareholder (with a value of not more than $10 million on August 31, 1982).

The conference agreement makes section 31(d)(2)(C) of present law applicable to distributions before January 1, 1986, of stock or securities pursuant to a judgment entered before July 23, 1982.

c. Stock purchases treated as asset purchases

Present law

Upon the complete liquidation of a subsidiary corporation, 80 percent of the voting power and 80 percent of the total number of shares of all other classes of stock (other than nonvoting preferred stock) of which is owned by the parent corporation, generally gain or loss is not recognized and the basis of the subsidiary's assets and the other tax attributes are carried over (secs. 332, 334(b)(1), and 381(a)).

If the controlling stock interest was acquired by purchase within a 12-month period and the subsidiary is liquidated pursuant to a plan of liquidation adopted within 2 years after the qualifying stock purchase is completed, the transaction is treated as in substance a purchase of the subsidiary's assets (sec. 334(b)(2)). The acquiring corporation's basis in the "purchased" assets is the cost of the stock purchased as adjusted for items such as liabilities assumed, certain cash or dividend distributions to the acquiring corporation, and postacquisition earnings and profits of the subsidiary. The liquidating distributions can be made over a 3-year period beginning with the close of the taxable year during which the first of a series of distributions occurs (sec. 332(b)(3)). Thus, this treatment applies even though the liquidation can extend over a 5-year period after control has been acquired.

In these cases, when the assets are treated as purchased by the acquiring corporation, recapture income is taxed to the liquidating corporation, the investment tax credit recapture provisions are applicable, and tax attributes, including carryovers, of the liquidated corporation are terminated.

Cases interpreting the law applicable before the rules in section 334(b)(2) were adopted treated the purchase of stock and prompt liquidation in some cases as a purchase of assets *(Kimbell-Diamond Milling Co.* v. *Commissioner* 14 T.C. 74, aff'd per curiam, 187 F.2d 718 (5th Cir.), cert. denied, 342 US 827 (1951)). It is not clear whether such treatment may still apply in some cases where the requirements of section 334(b)(2) are not met.

A stock purchase and liquidation is treated as a purchase of all the assets of the acquired corporation under present law if section 334(b)(2) applies. Revision of the special treatment of partial liquidations under the bill restricts the options of a corporate purchaser seeking to treat a purchase of a corporation as a purchase of assets in part combined with a continuation of the tax attributes of the acquired entity. Present law does not restrict a corporate purchaser from achieving such selectivity by purchasing assets directly from a corporation while concurrently purchasing the corporation's stock. Selectivity can also be achieved if an acquired corporation, prior to the acquisition, disperses its assets in tax-free transactions among several corporations which can be separately purchased.

The corporate purchaser then through selective qualifying liquidations can obtain asset purchase treatment for one or more acquired corporations while preserving the tax attributes of one or more other corporations.

House bill

No provision.

Senate amendment

In general

The Senate amendment repeals the provision of present law (sec. 334(b)(2)) that treats a purchase and liquidation of a subsidiary as an asset purchase. The bill is also intended to replace any nonstatutory treatment of a stock purchase as an asset purchase under the *Kimbell-Diamond* doctrine. Instead, an acquiring corporation, within 75 days after a qualified stock purchase, except as regulations may provide for a later election, may elect to treat an acquired subsidiary (target corporation) as if it sold all its assets in a complete liquidation on the stock acquisition date. The target corporation will be treated as a new corporation that purchased the assets on such date. Gain or loss will not be recognized to the same extent gain or loss is not recognized under present law (sec. 337) when a corporation sells all its assets in the course of a complete liquidation. This provision is intended to provide nonrecognition of gain or loss to the same extent that gain or loss would not be recognized under section 336 if there were an actual liquidation of the target corporation on the acquisition date to which present law section 334(b)(2) applied.[1]

A qualified stock purchase occurs if 80 percent or more of the voting power and 80 percent of the total number of shares of other classes of stock (except nonvoting, preferred stock) is acquired by purchase during a 12-month period (the acquisition period). The acquisition date is the date within such acquisition period on which the 80-percent purchase requirement (the qualified stock purchase) is satisfied.

The election is to be made in the manner prescribed by regulations and, once made, will be irrevocable.

Treatment of target corporation as new corporation

The assets of the target corporation will be treated as sold (and purchased) for an amount equal to the basis of the acquiring corporation in the stock of the target corporation on the acquisition date or, if the basis is greater on such date, on the last day of the 12-month acquisition period. The amount is to be adjusted under regulations for liabilities of the target corporation and other relevant items. It is anticipated that recapture tax liability of the target corporation attributable to the deemed sale of its assets is an item which may result in an adjustment under the regulations.

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[1] To the extent that Internal Revenue Service rulings providing that gain or income is not recognized by a liquidating insurance company with respect to its insurance reserves in a section 334(b)(2) liquidation constitute a proper interpretation of present law, gain or income is not recognized to the same extent upon an election to which new section 338 applies if the target corporation is an insurance company (see letter rulings 8112052 and 8150040).

The target corporation is treated as a 'new' corporation after the acquisition date for all purposes relating to its tax liability either as the selling or purchasing corporation. Its taxable year as the selling corporation ends on the date of acquisition and it does not become a member of the affiliated group including the acquiring corporation until the day following the date of acquisition. However, it is not intended that any minority shareholders in the target corporation shall be treated as having exchanged stock in the selling corporation for stock in the purchasing corporation. Further, additional purchases of the target corporation's stock by the acquiring corporation after the acquisition date are to be treated as purchases of the stock of the selling corporation if made on or before the close of the acquisition period.

Treatment of recapture items

Under the elective treatment provided by the bill, any recapture income of the target corporation attributable to the deemed sale of its assets is not to be included in any consolidated return of the acquiring corporation. The target corporation will not become a member of the acquiring corporation's affiliated group until the day following the date of acquisition. Recapture items of the target corporation will normally be associated with the final return of the target corporation (as the selling corporation) ending on the date of acquisition.

In some cases, recapture items may be includible in income for a period during which the target corporation is included in a consolidated return of the acquiring corporation. Where, for example, there is an adjustment to the purchase price for its stock based on post-acquisition date earnings of the target corporation, there may be additional amounts of recapture income. Such additional income is to be separately accounted for and may not be absorbed by losses or deductions of other members of the acquiring corporation's affiliated group.

Definition of purchase

The term "purchase" is defined as it is under present law (sec. 334(b)(3)) to exclude acquisitions of stock with a carryover basis or from a decedent, acquisitions in an exchange to which section 351 applies, and acquisitions from a person whose ownership is attributed to the acquiring person under section 318(a). Attribution under section 318(a)(4) relating to options will be disregarded for this purpose. However, if, as a result of a stock purchase, the purchasing corporation is treated under section 318(a) as owning stock in a third corporation, the purchasing corporation will be treated as having purchased stock in such third corporation but not until the first day on which ownership of such stock is considered as owned by the purchasing corporation under section 318(a).

A purchase of over 80 percent but less than 100 percent of the stock of a target corporation which in turn owns 80 percent of the stock of a third corporation is not a qualified stock purchase with respect to the third corporation because the purchasing corporation has not acquired by purchase the requisite 80 percent of the third corporation's stock. This is so, even though the purchasing corporation, the target corporation, and the third corporation constitute an affiliated group as defined in section 1504(a).

Consistency requirement

The rules require consistency where the purchasing corporation makes qualified stock purchases of two or more corporations that are members of the same affiliated group. For this purpose, purchases by a member of the purchasing corporation's affiliated group, except as regulations provide otherwise, are treated as purchases by the purchasing corporation.[2] The consistency requirement applies as well to a combination of a direct asset acquisition and qualified stock purchase.

The consistency requirement applies with respect to purchases over a defined "consistency period" determined by reference to the acquisition date applicable to the target corporation. The "consistency period" is the one-year period preceding the target corporation acquisition period plus the portion of the acquisition period up to and including the acquisition date, and the one-year period following the acquisition date. Thus, if all the target corporation's stock is purchased on the same day by the purchasing corporation, the one-year period immediately preceding and the one-year period immediately following such day are included in the consistency period. If, within such period, there is a direct purchase of assets from the target corporation or a target affiliate by the purchasing corporation, the rules require that the acquisition of the target corporation be treated as an asset purchase.

The consistency period may be expanded in appropriate cases by the Secretary where there is in effect a plan to make several qualified stock purchases or any such purchase and asset acquisition with respect to a target corporation and its target affiliates.

The consistency requirement is applied to an affiliated group with reference to a target corporation and any "target affiliate." A corporation is defined as a "target affiliate" of the target corporation if each was, at any time during that portion of the consistency period ending on the acquisition date of the target corporation, a member of an affiliated group that had the same common parent. An affiliated group has the same meaning given to such term by section 1504(a) (without regard to the exceptions in sec. 1504(b)). This definition also applies in determining whether a purchase is made by a member of the same affiliated group as the purchasing corporation.

An acquisition of assets from a target affiliate during the consistency period applicable to the target corporation will require the qualified stock purchase of the target corporation to be treated as a purchase of assets. In applying these rules, stock in a target affiliate is not to be treated as an asset of any other target affiliate or of the target corporation.

In applying these rules, acquisitions of assets pursuant to sales by the target corporation or a target affiliate in the ordinary course of its trade or business and acquisitions in which the basis of assets is carried over will not cause the consistency requirement to apply. The sale by a target corporation will be considered as a sale in the ordinary course of business for this purpose even though it is not customary in the course of the selling corporation's business provided it is a transaction that is a normal incident to the conduct of a trade or business, such as a sale of used machinery that was employed in the seller's trade or business.

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[2] This rule will prevent transfers of target corporation stock within the purchasing corporation's affiliated group from disqualifying a section 338 election (*Chrome Plate, Inc.* v. *U.S.*, 614 F.2d 990 (5th Cir. 1980).

Where there are, within a consistency period, only qualified stock purchases of the target corporation and one or more target affiliates by the purchasing corporation, an election with respect to the first purchase will apply to the later purchases. A failure to make the election for the first purchase will preclude any election for later purchases.

To prevent avoidance of the consistency requirements, the bill authorizes the Secretary to treat stock acquisitions pursuant to a plan and satisfying the 80-percent requirement to be treated as qualified stock purchases even though they are not otherwise so defined. For example, an acquiring corporation may acquire 79 percent of the stock of a target corporation and, within a year, purchase assets from such corporation or a target affiliate planning to purchase the remaining target corporation stock more than one year after the original stock purchase. The Secretary may under these circumstances treat the purchase of the target corporation's stock as a deemed sale of its assets by the target corporation. The bill also authorizes such regulations as may be necessary to ensure that the requirements of consistency of treatment of stock and asset purchases with respect to a target corporation and its target affiliates are not circumvented through the use of other provisions of the law or regulations, including the consolidated return regulations.

The Senate amendment applies to qualified stock purchases of a target corporation where the acquisition date occurs after August 31, 1982. However, in any case where the acquisition date occurs after December 31, 1981, and before September 1, 1982, the purchasing corporation may elect on or before November 15, 1982, to have section 338 apply.

Conference agreement

The conference agreement follows the Senate amendment with technical modifications. The conference agreement expressly provides that the target corporation will be treated as having sold all its assets at the close of the acquisition date in a single transaction to which section 337 applies and, as the 'new' corporation, will be treated as having purchased all the assets at the beginning of the day following the acquisition date. This amendment provides an explicit statutory rule clarifying the intent of the Senate amendment that the deemed sale is reported on the return of the 'old' corporation and that it is only the 'new' corporation that becomes a member of the purchasing corporation's affiliated group.

The conference agreement modifies the provisions of the Senate amendment which treat the amount for which the target corporation's assets are deemed to be sold (and purchased) by reference to the acquiring corporation's basis in the stock of the target corporation. Under the conference agreement, if the acquiring corporation owns less than 100 percent by value of the target corporation's stock on the acquisition date, the deemed purchase price is grossed up to equate 100-percent ownership by the acquiring corporation and the nonrecognition of gain or loss to the target corporation is limited, unless the target corporation is liquidated within one year after the acquisition date, to the highest actual percentage by value of target corporation stock held during the one-year period beginning on the acquisition date.

The conference agreement provides that if, in connection with a qualified stock purchase with respect to which an election is made, the target corporation makes a distribution in complete redemption of all the stock of a shareholder (other than the acquiring corporation), section 336 of the Code will apply to the distribution as if it were made in a complete liquidation. This will preclude gain from being recognized to the target corporation under the provisions relating to stock redemptions by a continuing corporation.

Under the conference agreement, if the acquisition date with respect to a target corporation was after August 31, 1980, and before September 1, 1982, and the target corporation was not liquidated before September 1, 1982, the purchasing corporation may make an election under new section 338(a).

At the election of the purchasing corporation, section 338 as added by the bill will not apply to any acquisition made pursuant to a contract binding on July 23, 1982, to acquire control (within the meaning of sec. 368(c)) of any financial institution where completion of the acquisition is subject to approval by one or more regulatory authorities and a plan of complete liquidation of one or more corporations acquired pursuant to such contract is adopted within 90 days after the date of final approval of the last such regulatory authority granting final approval.

Under the conference agreement, except as provided in regulations and subject to such conditions as may be provided in regulations, the term 'target affiliate' does not include a foreign corporation or a DISC ORGA corporation to which section 934(b) or section 936 applies, and the consistency rules do not apply to stock held by a target affiliate in a foreign corporation or a domestic corporation which is a DISC or which is described in section 1248(e).

Under the conference agreement, the acquisition of assets before September 1, 1982, and, to the extent provided under regulations, foreign held assets will not result in a deemed section 338 election with respect to a target corporation.

The conference agreement provides regulatory authority pursuant to which the Secretary may determine that the deemed election will not apply as the result of a *de minimis* acquisition of assets and may also preclude the application of the deemed election rule if it is determined that the taxpayer has acquired assets in order to avoid the 75-day limit on the period after the acquisition date within which the election must be made.

d. Reorganizations constituting changes in form

Present law

A reorganization includes "a mere change in identity, form, or place of organization" (an F reorganization). Generally, present law requires a transferor corporation's taxable year to be closed on the date of a reorganization transfer and precludes a post-reorganization loss from being carried back to a taxable year of the transferor. However, F reorganizations are excluded from these limitations in recognition of the intended scope of such reorganizations as embracing only formal changes in a single operating corporation.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement limits the F reorganization definition to a change in identity, form, or place of organization of a single operating corporation.

This limitation does not preclude the use of more than one entity to consummate the transaction provided only one operating company is involved. The reincorporation of an operating company in a different State, for example, is an F reorganization that requires that more than one corporation be involved.

The amendment applies to transactions occurring after August 31, 1982. Present law continues to apply to plans of reorganization adopted before August 31, 1982, provided the transaction is completed by December 31, 1982.

e. Use of holding companies to bail out earnings

Present law

Shareholders who have their stock redeemed in a corporate distribution not in partial or complete liquidation are entitled to sale or exchange treatment rather than dividend treatment generally only if the transaction results in a termination or substantial reduction in the proportionate interests of the redeeming shareholders. Where the same shareholder or a group commonly controls two or more corporations, they may attempt to avoid the dividend consequences that would result from a pro rata redemption of stock by selling the stock in one controlled corporation to another. Present law (sec. 304) deals with this effort to avoid dividend treatment by testing the tax consequences of the transaction as if the shareholders had their stock redeemed by the corporation whose stock is sold.

Shareholders have attempted to avoid the present law rules by borrowing funds secured by the stock of a corporation with earnings and profits and contributing the stock to a newly formed holding company in exchange for the holding company's stock plus its assumption of the liability for the borrowed funds. Taxpayers argue that the transaction complies with present law rules governing tax-free incorporation of property. These rules overlap with those requiring stock sales to a commonly controlled corporation to be tested as stock redemptions. The courts are divided as to which provision controls. It is also unclear whether section 304 applies where the holding company is a newly formed corporation. Even if the redemption rule applies and dividend treatment results, dividend consequences would be determined by reference to the earnings of the purchasing corporation. If it is a newly formed holding company, it would have no earnings (a pre-existing corporation without earnings could also be used).

Another device to bail out earnings is to cause a corporation to issue preferred stock as a nontaxable stock dividend to its shareholders. A sale of the preferred stock at capital gain rates would not dilute the interests of the selling shareholders in future corporate growth while they would receive an amount representing corporate earnings. Preferred stock issue under these circumstances (described as section 306 stock) is tainted under present law so that its subsequent sale or redemption results in ordinary income to the shareholder. This provision does not taint stock of a newly formed corporation issued in a tax-free transaction in exchange for stock in a corporation with earnings and profits. Thus, creation of a holding company issuing both common and preferred stock offers the same bail-out opportunity as a preferred stock dividend but does not result in tainted section 306 stock.

House bill

No provision.

Senate amendment

No provision.

The conference agreement extends the anti-bailout rules of sections 304 and 306 of present law to the use of corporations, including holding companies, formed or availed of to avoid such rules. Such rules are made applicable to a transaction that, under present law, otherwise qualifies as a tax-free incorporation under section 351.

Section 351 generally will not apply to transactions described in section 304. Thus, section 351, if otherwise applicable, will generally apply only to the extent such transaction consists of an exchange of stock for stock in the acquiring corporation. However, section 304 will not apply to debt incurred to acquire the stock of an operating company and assumed by a controlled corporation acquiring the stock since assumption of such debt is an alternative to a debt-financed direct acquisition by the acquiring company. This exception for acquisition indebtedness applies to an extension, renewal, or refinancing of such indebtedness. The provisions of section 357 (other than sec. 357(b)) and section 358 apply to such acquisition indebtedness provided they would be applicable to such transaction without regard to section 304. In applying these rules, indebtedness includes debt to which the stock is subject as well as debt assumed by the acquiring company.

Under the conference agreement, section 306 is made applicable to preferred stock acquired in a section 351 exchange if, had money in lieu of stock been received, its receipt would have been a dividend to any extent. This, if the receipt of cash by the shareholder rather than stock would have caused section 304 as amended by the bill, rather than section 351, to apply to such receipt, some or all of the amount received might have been treated as a dividend.

In such a case, the preferred stock acquired in the exchange will be section 306 stock.

To the extent of any amount distributed (including any liability assumed or to which the stock is subject) in an exchange for stock to which section 304(a)(1) applies, the earnings and profits of the issuing corporation, to the extent thereof, will be deemed to be distributed to the acquiring company. This rule also applies in determining whether preferred stock acquired in a section 351 exchange is section 306 stock. For this purpose, the property is deemed distributed by the issuing to the acquiring corporation and thereafter distributed to the exchanging shareholders. The deemed distribution is solely for the purpose of determining the extent to which the amount distributed is treated as a dividend to such shareholders and does not, for example, constitute a distribution of personal holding company income to the acquiring corporation.

In determining whether corporations are commonly controlled for purposes of section 304, all shareholders transferring stock to a holding company would be counted even though some of them do not receive property other than stock.

An exception would apply to the receipt of securities in a bank holding company by certain minority shareholders. Under this rule, the transfer of stock constituting control of a bank to a bank holding company in connection with the formation of such company (unless such company is formed before 1985) must be made within 2 years after control of such bank was acquired. Both acquisition of control of the bank and the transfer of its stock constituting control to the bank holding company must be pursuant to a plan. Further, distributions of property (as described in sec. 304(a)) incident to the formation of such bank holding company may be made only to shareholders who, in the aggregate, do not have stock constituting control of such company.

If the above conditions are satisfied, section 304(a) will not apply to securities received, incident to the formation of the bank holding company, by any shareholder who owns less than 10 percent in value of the stock of such company.

Control, for purposes of applying this exception, means control as defined in section 304(c)(1) and ownership is to be determined under the rules in section 304(c)(3). A bank holding company is a bank holding company within the meaning of the Bank Holding Company Act.

The amendments made by the conference agreement apply to transfers occurring after August 31, 1982, in taxable years ending after such date. However, if an application was filed with the Federal Reserve Board before August 16, 1982, to form a bank holding company, the amendments will not apply to transfers by a bank holding company formed pursuant to approval of such application if such transfers are made before January 1, 1983, or (if later) within 90 days after the last final required regulatory approval of such formation.

f. Application of attribution rules

Present law

To determine whether a shareholder is entitled to sale or exchange treatment on a stock redemption, stock held by related parties is attributed to the shareholder in determining whether the shareholder's interest in the corporation was terminated or significantly reduced. The attribution rules do not apply to some transactions that are economically equivalent to straight stock redemptions and that offer an equivalent opportunity to bail out earnings. For example, a shareholder may exchange all of his common stock in a corporation for preferred stock. Such an exchange results in tainted, section 306 stock only if, had cash been distributed in lieu of preferred stock, there would have been a dividend. Unless stock held by another family member or controlled entity is attributed to the shareholder, cash in lieu of preferred stock would have terminated the shareholder's interest and not result in a dividend. Also, a shareholder exchanging stock in a reorganization for property other than stock or securities may have dividend consequences if the transaction has the effect of the distribution of a dividend. For this purpose, attribution rules do not apply.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement extends the ownership attribution rules to a determination of whether, for section 306, the effect of the receipt of preferred stock pursuant to a reorganization or a transaction described in section 355 or section 351 is substantially the same as a dividend and in determining whether the receipt of property in a reorganization has the effect of a dividend. Attribution between shareholders and corporations shall be applied without regard to the 50-percent limit in section 318(a)(2)(C) and 318(a)(3)(C) in applying such rules to the receipt of preferred stock in a section 351 exchange.

The application of constructive ownership rules to section 306 determinations applies to stock received after August 31, 1982, in taxable years ending after such date. Application of such rules to the determination of whether the receipt of property pursuant to a reorganization has the effect of a dividend applies to distributions after August 31, 1982, in taxable years ending after such date.

g. Waiver of family attribution rules

Present law

In determining whether a shareholder has completely terminated his interest in a corporation on a stock redemption so as to achieve sale or exchange treatment, present law allows the shareholder to waive attribution of ownership from other family members. The waiving shareholder in general may hold no interest in the corporation (except as a creditor), may not acquire any interest for a 10-year period, and must agree to notify the Internal Revenue Service of any such acquisition. The statute of limitations for the year of redemption remains open in the event of such an acquisition.

Stock may be attributed from one member of a family to another by family attribution and reattributed to an entity such as an estate or trust in which the constructive owner has a beneficial interest. The Internal Revenue Service takes the position that only an individual may waive family attribution. Several decided cases have held that a trust or an estate terminating its interest by a stock redemption can waive family attribution from a family member to the beneficiary. These cases do not preclude the beneficiary from acquiring an interest in the corporation, do not require an agreement from the beneficiary, and do not reopen the statute of limitations in the event of an acquisition by the beneficiary. One case has also held that an entity may waive attribution from a beneficiary to the entity.

House bill

No provision.

Senate amendment

No provision

Conference agreement

The conference agreement permits an entity to waive the family attribution rules if those through whom ownership is attributed to the entity join in the waiver. Thus, a trust and its beneficiaries may waive family attribution to the beneficiaries if, after the redemption, neither the trust nor the beneficiaries hold an interest in the corporation, do not acquire such an interest within the 10-year period, and join in the agreement to notify the IRS of any acquisition. The entity and beneficiaries would be jointly and severally liable in the event of an acquisition by any of them within the 10-year period and the statute of limitations would be open to assess any deficiency. The tax increase would be a deficiency in the entity's tax but would be asserted as a deficiency against any beneficiary liable under the rules. The conferees intend that the tax will be collected from a beneficiary only when it cannot be assesed against or collected from the entity, such as when the entity no longer exists or has insufficient funds. Further, it is intended that the tax will be assessed and collected from the beneficiary whose acquisition causes the deficiency before it is asserted against any other beneficiary.

Under the bill, only family attribution under section 318(a)(1) may be waived by an entity and its beneficiaries. The waiver rules would not be extended to waivers of attribution to and from entities and their beneficiaries (secs. 318(a)(2) and 318(a)(3)). The bill thus is intended to overrule *Rickey* v. *United States* 592 F.2d 1251 (5th Cir. 1979). The conferees intend that the bill should not be construed to provide any inference as to whether the *Rickey* decision adopts a proper construction of present law. Nor is any inference intended as to whether the other cases extending the waiver rules for family attribution to entities adopt a proper construction of present law.

Certain anti-avoidance rules of present law applicable where a related party at the time of the redemption owns stock acquired from the distributee would be extended to the entity and affected beneficiaries.

These amendments apply with respect to distributions after August 31, 1982, in taxable years ending after such date.

10. Accounting for completed contracts

Present law

Overview

A taxpayer who enters into long-term contracts may elect to use one of four accounting methods to account for the income and expenses attributable to such contracts. Long-term contracts generally are building, installation, construction, or manufacturing contracts that are not completed by the end of the taxable year in which they were entered into. A manufacturing contract is not a long-term contract unless it involves the manufacture of either (1) unique items of a type not normally carried in the finished goods inventory of the taxpayer or (2) items that normally require more than 12 months to complete.

The four methods used to account for long-term contracts are the cash method, the accrual method, the percentage of completion method and the completed contract method. The cash and accrual methods are methods applicable to all types of income of all taxpayers generally. The percentage of completion method and the completed contract method apply only to long-term contracts.

Cash method

Under the cash method, income is reported for the year in which it is actually or constructively received. Deductions generally are taken for the year in which actually paid.

Accrual method

Under the accrual method, income is generally reported when all the events have occurred which fix the right to receive such income and the amount thereof can be determined with reasonable accuracy, regardless of when it is received. Taxpayers are not required, however, to report income at the time advance payments are received under long-term contracts, but generally may report such income when the subject matter of the contract is shipped, delivered, or accepted.

Deductions generally are allowed for the year in which all events have occurred which determine the fact of liability and the amount thereof can be determined with reasonable accuracy. However, any expenditure which results in the creation of an asset having a useful life which extends substantially beyond the close of the taxable year may not be deductible, or may be deductible only in part, for the taxable year in which incurred. If the taxpayer uses inventories, costs allocable to inventory are accumulated until the inventory is shipped, delivered, or accepted.

Percentage of completion method

Under the percentage of completion method (which is used only for long-term contracts), income is recognized according to the percentage of the contract that is completed during each taxable year. Deductions generally are allowed in the year in which they are incurred.

Completed contract method

Recognition of income and deductions.—Under the completed contract method (which is used only for long-term contracts), income and costs from the contract generally are reported for the year in which the contract is completed.

Completion of contract.—Present Treasury regulations (sec. 1.451-3) provide that a contract will not be considered completed until final completion and acceptance have occurred. Nevertheless, a taxpayer may not delay completion of a contract for the principal purpose of deferring Federal income tax.

Severance and aggregation of contracts.—Present Treasury regulations also provide that it may be necessary to treat one agreement as several contracts or several agreements as one contract in order to clearly reflect the income of the taxpayer. Whether one agreement is severed or several agreements are aggregated depends on all the facts and circumstances.

Allocation of costs.—Under the completed contract method, costs allocable to the contract (commonly referred to as "contract costs") are deductible for the year in which the contract is completed. Expenses that are not allocated to the contract (commonly referred to as "period costs") are deductible for the year in which they are paid or incurred.

Under existing regulations, contract costs include all direct expenses and indirect expenses that are incident and necessary to the performance of the contract, with the following exceptions (which are currently deductible as period costs):

(a) Marketing and selling expenses, including bidding expenses;

(b) Advertising expenses;

(c) Other distribution expenses;

(d) General and administrative expenses which benefit the taxpayer's business as a whole;

(e) Interest;

(f) Research and development expenses;

(g) Losses, under section 165 and the regulations thereunder;

(h) Percentage depletion in excess of cost depletion;

(i) Depreciation on idle equipment and, for other equipment, tax depreciation in excess of book depreciation;

(j) Income taxes;

(k) Pension and profit-sharing contributions and other employee benefits;

(l) Costs attributable to strikes, rework, scrap, and spoilage; and

(m) Officer compensation which benefits the taxpayer's activities as a whole.

House bill

No provision.

Senate amendment

Completion of contract

The Treasury Department would amend its regulations to prevent unreasonable deferral of recognition of income by reason of contract provisions that are merely incidental to contract obligations for construction, installation, or manufacturing.

The revised rules apply to taxable years ending after December 31, 1982. Contracts that would be treated as completed in an earlier taxable year solely by reason of the revised termination rule would be treated as completed in the first taxable year ending after December 31, 1982.

Severing and aggregating contracts

The Treasury Department would amend its regulations to prevent the unreasonable deferral of recognition of income by reason of the taxpayer's treating several contracts as a single contract (for example, where the items to be constructed, installed, or manufactured under the contracts are independently priced and will be separately delivered or accepted).

The revised severance and aggregation rules apply to taxable years ending after December 31, 1982. A contract that would have been completed in an earlier taxable year if it had been severed from a group of contracts under the revised rules will be considered completed when the first contract of the same group is completed after December 31, 1982.

Allocation of costs

For long-term contracts expected to be completed within 2 years and certain other construction contracts, present law cost allocation rules will continue to apply. Construction contracts eligible for continued use of present law costing rules are contracts for the construction of real property improvements (or installation of integral components thereof) if either—

(1) the contract is expected to be completed within 3 years, or

(2) the taxpayer has average annual gross receipts of $25 million or less for the prior 3 years.

In the case of a contract for the manufacture and installation of an improvement to real property, the special cost allocation rules for construction contracts apply to only the costs related to the installation of the real property improvements. For purposes of determining whether such a contract is expected to be completed within 3 years, the time expected to complete both the manufacture and installation of the property will be taken into account.

For all other contracts (extended period long-term contracts), costs that arise from or directly benefit such contract activities of the taxpayer are to be treated as contract costs. For extended period long-term contracts, the following costs will *no longer* be period costs:

(1) Bidding expenses on contracts awarded to the taxpayer;

(2) Distribution expenses, such as shipping costs;

(3) General and administrative expenses properly allocable to long-term contracts under regulations to be prescribed by the Secretary;

(4) Research and development expenses that either are directly attributable to particular long-term contracts existing when the expenses are incurred or are incurred under an agreement to perform research and development;

(5) Depreciation, capital cost recovery, and amortization for equipment and facilities currently being used, to the extent it exceeds depreciation reported by the taxpayer for financial accounting purposes;

(6) Pension and profit-sharing contributions representing current service costs and other employee benefits;

(7) Rework labor, scrap, and spoilage; and

(8) Percentage depletion in excess of cost depletion.

The revised cost allocation rules apply to contracts entered into after December 31, 1982, for taxable years beginning after December 31, 1982, with a phase-in.

Under the phase-in, a percentage of the additional costs allocable to the contract under the revised rules would be currently deductible. The percentages are:

For taxable year beginning in—	*The currently deductible percentage is*
1983	66⅔
1984	33⅓
1985 and thereafter	0

Conference agreement

The conference agreement follows the Senate amendment.

11. Accelerated corporate tax payments

Present law

Corporations generally must pay 80 percent of their current year's tax liability in quarterly estimated tax payments during the taxable year.

A penalty for underpayment of estimated taxes is imposed unless the corporation meets certain exceptions based on prior year's tax liability, prior year's income or annualized income. At each installment date, annualized income is projected from the actual taxable income earned by the end of the previous month (or quarter). Under present annualization rules, corporations with seasonal income earned primarily at the beginning of the year may upon occasion overpay estimated taxes due when they rely on the annualized income exception.

Generally, a corporation must pay its final tax payment 2½ months after the end of the taxable year, but it may elect to pay only half of the unpaid tax on this date and the remaining half three months later.

House bill

No provision.

Senate amendment

The amount of estimated tax payments required for all corporations is increased from 80 percent to 90 percent of current year's tax liability. A corresponding change will be made in the exception based on annualized income.

The penalty on underpayments of estimated tax that are between 80 percent and 90 percent of the actual tax due is imposed at one-half the full rate for underpayments.

The full amount of the unpaid tax is due 2½ months after the end of a taxable year.

Conference agreement

The conference agreement generally follows the Senate amendment, with three changes.

First, the penalty for underpayment of estimated taxes is imposed at three quarters of the full rate on underpayments between 80 and 90 percent of the tax due, but only if the taxpayer makes estimated tax payments of at least 80 percent of the tax due.

Second, a new rule for annualizing income is provided for corporations with seasonal income. Taxpayers could rely on the new rule if, in the preceding three taxable years, taxable income for any period of 6 successive months averaged 70 percent or more of total income for the taxable year. Income would be annualized by assuming that the income is earned, in the current year, in the same pattern as in the three preceding taxable years. This rule would require that the tax be paid on the annualized income in the same seasonal pattern in which it is earned.

Third, for the annualized income exceptions, the Treasury is directed to amend its regulations regarding the computation of taxable income for the period before the installment due date. Taxpayers could rely on these regulations in computing taxable income for a period of less than a full taxable year under the annualization and seasonal pattern of income exceptions to the underpayment penalty. Many items which substantially impact taxable income cannot be determined accurately by the installment due date. Examples of these items include (but are not limited to) the LIFO index for taxpayers using the dollar-value LIFO inventory method, the deferred gross profit for taxpayers with revolving charge accounts, intercompany adjustments for taxpayers who file consolidated returns, and a temporary liquidation of a LIFO layer at the installment date.

To alleviate these problems for taxpayers who rely on the annualized income exception, the conferees expect the Secretary to issue regulations which provide that estimates of certain items could be used where reasonable estimates could be made from existing data. For example, taxpayers using the dollar-value LIFO method of accounting might be allowed to interpolate from an available inflation index for a previous period in calculating the cost of goods sold in a period of less than a full taxable year if no reliable inflation index is available for the period for which taxable income must be calculated. The conferees also understand that the Secretary will issue regulations clarifying the meaning of taxable income in regard to net operating loss carrybacks and carryforwards for purposes of defining a large corporation (under sec. 6655 (h) (2)).

12. Amortization of original issue discount on bonds

Present law

Original issue discount on corporate bonds is included in income by holders in whose hands such bonds are capital assets, and is allowed as a deduction to the issuer, on a linear basis over the life of the bond. The discount is treated as accruing in equal monthly installments over the life of the bond. The OID provisions of the Internal Revenue Code do not provide for ratable inclusion of discount income by holders of noncorporate bonds. A portion of gain from the sale or disposition of government bonds is treated as ordinary income to the extent of accrued original issue discount.

House bill

No provision.

Senate amendment

The Senate amendment provides new rules under which the inclusion and deduction of original issue discount correspond to the actual economic accrual of interest. These rules are extended to bonds issued by noncorporate issuers other than natural persons.

The Senate amendment applies to corporate obligations issued after May 3, 1982 (other than obligations issued pursuant to a written commitment which was binding on such date). The extension of the rules to obligations of noncorporate issuers applies to obligations issued after June 9, 1982 (other than obligations issued pursuant to a written commitment which was binding on such date).

Conference agreement

Under the conference agreement, the new rules applicable under the Senate amendment to original issue discount on corporate obligations and the extension of such rules to noncorporate obligations are effective for obligations issued after July 1, 1982, unless issued pursuant to a written commitment binding on July 1, 1982, and at all times thereafter. Such a commitment would have to involve a commitment by the issuer to issue the bonds at a particular price. Thus, for example, the new rules would not apply in cases where bonds are issued pursuant to the exercise of warrants which were outstanding on July 1, 1982.

A technical amendment makes explicit that tax-exempt obligations are excepted from the rules even if the exemption is provided by a provision of law other than section 103.

Certain tax-exempt industrial development bonds generate interest deductions for a taxable issuer. An amendment makes clear that the deduction of original issue discount on such obligations will be subject to the new rules.

13. Tax treatment of stripped bonds

Present law

If a taxpayer disposes of a bond and retains the unmatured interest coupons or disposes of the bond and the coupons in separate transactions, it is arguable that the taxpayer's basis is entirely allocable to the corpus (bond principal). Any loss from disposing of the corpus, if allowable, is an ordinary loss to a dealer in such obligations, or to a bank, and a capital loss to other taxpayers.

Gain to the purchaser of a stripped bond is deferred until the bond is sold or redeemed and is ordinary income to the extent of the difference between the value of the bond with and without the coupons attached at the time of purchase. The purchaser of stripped coupons allocates his cost to the coupons in accordance with their relative values at the time of purchase. Capital gain may result if coupons are sold rather than redeemed.

House bill

No provision.

Senate amendment

Stripped bonds and stripped coupons in the hands of a purchaser are treated as bonds issued at a discount. The discount is the excess of the redemption price of the bond, or amount payable on maturity of the coupon, over the purchase price allocable to the bond or coupon. The purchaser must include the discount in income under the original issue discount rules.

The seller of a stripped bond or stripped coupons must, immediately before the disposition, allocate the basis of the bond (with coupons) among the bond and coupons in accordance with their values. This will prevent artificial losses from the sale of stripped bonds. The same original issue discount treatment applicable to a buyer of a stripped bond or stripped coupons applies to the retained portions after a seller strips and disposes of either the corpus or coupons.

The treatment of stripped bonds applies with respect to the purchase and sale of a stripped bond or stripped coupons after June 9, 1982.

Conference agreement

The conference agreement follows the Senate amendment with a different effective date. Under the conference agreement, the new treatment applicable to coupon stripping under the Senate amendment applies only where there is a sale after July 1, 1982, of either a stripped bond or stripped coupons.

The conference agreement provides that accrued interest required by the new rules to be included in income upon the disposition of a stripped bond or stripped coupons does not include any interest theretofore included in income by the taxpayer (e.g., by an accrual basis taxpayer).

The rule of present law that requires ordinary income treatment on the sale or other disposition of a stripped bond to the extent of the difference in fair market value of the bond with and without coupons attached at the time of purchase is continued for bonds purchased at any time before July 2, 1982. As under the Senate amendment, this rule is applicable to tax-exempt obligations without regard to the date of purchase. In applying this rule, a technical amendment clarifies that a person who retains a tax-exempt bond after disposition of the coupons will be treated as a purchaser of a stripped tax-exempt bond.

Another technical amendment provides that the definition of 'coupon' as any right to receive interest on a bond whether or not evidenced by a coupon will apply only where a purchase occurs after July 1, 1982. This amendment is not intended to provide any inference as to the interpretation of the term 'coupon' in present law section 1232(c).

The conference agreement also provides the Secretary of the Treasury with the authority to issue regulations to provide the appropriate basis allocation and income inclusion rules in cases where the general rules in the statute do not provide a proper determination of income by reason of call provisions, extendable maturities, etc. For example, in the case of callable bonds with coupons redeemable after the call date, these regulations could provide that no basis need be allocated to post-call coupons as long as they remain attached to the corpus and that there be no periodic inclusion of discount income with respect to post-call coupons where this is appropriate.

14. Treatment of business meal expenses and tip income

Present law

Business meals

In general, expenditures for business meals are deductible to the extent that they are ordinary and necessary, not extravagant or lavish, and are paid or incurred in connection with the taxpayer's trade or business or income-producing activities.

Tip income

Tipped employees must generally report all tips received in the course of their employment to their employer.

In general, withholding for purposes of the Federal Insurance Contributions Act (FICA) tax and the income tax is required only to the extent tips are reported to the employer and only to the extent collection of the tax can be made by the employer from wages paid to the employee (excluding tips, but including funds turned over by the employee to the employer or under the control of the employer).

In general, employees whether or not they receive tips, are required to keep records to establish the amount of gross income and deductions. Because tips are includible in income, employees must keep records of all tips received and of all deductible tips paid to other employees. Employers are expressly required to retain only charge tip receipts and statements of tips received by employees furnished by such employees. Failure to maintain such records may subject employees or employers to penalties (sec. 6653).

House bill

No provision.

Senate amendment

Any deduction otherwise allowable for business meals and beverages (unless connected with business-related travel away from home) is limited to 50 percent of expenses. This provision is effective for taxable years beginning after December 31, 1982.

Conference agreement

The conference agreement does not include the Senate amendment relating to business meals expense deduction.

Under the conference agreement, the rules of present law relating to reporting of tips to employers by their employees and to the resulting withholding of FICA and income taxes is retained. However, to assist the Internal Revenue Service in its examinations of returns filed by tipped employees, the bill provides a new set of information reporting requirements for large food and beverage establishments and, under certain circumstances, a tip allocation requirement.

Each large food and beverage establishment will be required to report annually to the Internal Revenue Service (1) the gross receipts of the establishment from food and beverage sales (other than receipts from carryout sales and mandatory 10-percent or more service charge sales), (2) the amount of aggregate charge receipts (other than receipts from carryout sales and 10-percent service charge sales), (3) the aggregate amount of tips shown on such charge receipts and (4) reported tip income and mandatory service charges of less than 10 percent. Tips on meals charged for house charges of restaurants will be reported. Tips on meals charged to a room in a hotel, however, will be reported as gross receipts only.

If the employees voluntarily report tips aggregating 8 percent or more of gross receipts (defined as gross receipts less carryout sales, less 10-percent service charge sales), then no tip allocations, will need to be made. However, if this 8-percent reporting threshold is not met, then the employer must allocate an amount equal to the difference between 8 percent of gross receipts and the amounts reported by employees for the year to all tipped employees pursuant to either an agreement between the employer and employees or in the absence of such an agreement according to regulations issued by the Secretary. The conferees intend that the regulations under this provision will provide procedures under which a particluar establishment, or type of establishment, can show that its tipped employee's average tip rate is less than 8 percent (but not less than 5 percent) and, therefore, allocate based on that lower amount in the future. The employer will have no liability in connection with any dispute regarding tip allocations.

The allocation of the 8-percent amount to employees for reporting purposes will have no effect on the FICA or income tax withholding responsibilities of the employer or on his FUTA obligations. Thus, employers will continue to withhold only on amounts reported to them by their tipped employees. Of course, the allocation also has no effect on the actual entitlement of the employer or employee to gross receipts or tip income. Similarly, this purely informational report to the Internal Revenue Service will not affect the requirements of the Fair Labor Standards Act or any collective bargaining agreement.

The 8-percent figure reflects the conferees' judgment that the tip rate in establishments subject to this reporting requirement will rarely be below the 8-percent level. Thus, an employee who reports less than his allocated amount of tips must be able to substantiate his reporting position with adequate books and records (as he must under present law). The Internal Revenue Service could prove that tipped employees received a larger amount of tip income. For example, as under present law, the Internal Revenue Service could show from charge tip rates that a particular establishment had a higher tip rate than 8 percent.

A large food or beverage establishment is any establishment (public or private) the activity of which is the provision of food or beverages for consumption on the premises, other than of a "carryout" nature such as "fast food restaurants," with respect to which tipping is customary, and which normally employed more than 10 employees on a typical business day during the preceding calendar year. The Secretary will prescribe regulations for the application of this 10-employee rule in the case of new businesses. Thus "fast-food" restaurants would not generally be subject to the new reporting requirement. Restaurants that provide table or counter service for seated customers, and cocktail lounges with similar service, are large food or beverage establishments if they employ 10 or more persons. An establishment may be part of a larger operation such as a hotel.

It is anticipated that the information statement concerning allocated tips could be integrated into Form W-2 now supplied by employers with respect to wages. If the employer furnishes an employee with a W-2 within 30 days after the employee leaves, the employer must furnish the employee and the IRS in January with an amended Form W-2 that includes tip allocations.

The conference agreement requires the Secretary of the Treasury to submit, prior to January 1, 1987, to the tax writing committees of the Congress a report together with the background study on the operation of the present reporting system as applied to tips received as wages or compensation. This report should be based upon a study conducted by the IRS designed to statistical accuracy with an error of plus or minus of 15 percent. The study should be representative of the foodservice industry in terms of sales size and types of establishments. This study should also specifically describe the following: (1) the amount of tips actually received; (2) the amount of tips voluntarily reported to the employer by the employee; (3) the amount of tips reported to the IRS on the individual's federal tax return; and (4) a computation of the minimum wage payments to these individuals and what portion of those wages constituted tip income.

This study should further describe tipped individuals by job category, and should distingush between part-time and full-time employment. The study should also describe the extent of arrangements for tip sharing and tip pooling that exist among tip earners. Recommendations made by the Internal Revenue Service as a result of this study should contain a cost-benefit analysis of any recommendations. This analysis should include a comparison of the cost of the existing system of enforcement of tip earner compliance through examination and any cost increase or decrease to the government if any recommendation is adopted.

The amendments made by this section apply to calendar years beginning after December 31, 1982, but the allocation rules will first apply to payroll periods ending after March 31, 1983. For the first quarter of calendar year 1983 only, large food and beverage establishments for which aggregate tip income reported by employees is less than 8 percent of such gross food and beverage sales, will be required to file information returns for that quarter for Internal Revenue Service audit purposes. These returns shall include a list of al tipped employees including their taxpayer identification numbers, wages paid and reported tip income during the period. Employees would be put on notice that their returns would be identified for audit unless this 8 percent tip reporting is satisfied.

15. Investment credit for soil or water conservation expenditures

Present law

Soil or water conservation expenditures equal to up to 25 percent of gross income from farming may be deducted during the year incurred instead of being charged to capital account, at the election of the taxpayer. A taxpayer may not elect to treat as deductible expenditures those items for which depreciation deductions may be claimed.

Present law includes no special investment credit for soil and water conservation expenditures.

House bill

No provision.

Senate amendment

The Senate amendment permits farmers to elect a 10-percent investment credit for those soil and water conservation expenditures that are not expensed. The provision applies to periods after December 31, 1982.

Conference agreement

The conference agreement does not include the Senate amendment.

16. Public utility dividend reinvestment plans

Present law

Under present law, public utility corporations may set up dividend reinvestment plans under which shareholders electing to receive distributions in the form of common stock, rather than money or other property, may exclude up to $750 per year ($1,500 in the case of a joint return) of the stock distribution from income. These amounts generally are taxed as capital gains when the stock is sold, if the stock has been held for at least 12 months.

The provision applies to distributions made after 1981 and before 1986.

House bill

No provision.

Senate amendment

Under the Senate amendment, the provision is repealed for distributions made after December 31, 1982.

Conference agreement

The conference agreement does not include the Senate amendment.

C. Compliance Provisions

1. Withholding on interest and dividends

Present law

Under present law, no income tax withholding is required on payments of interest, dividends, or patronage dividends to U.S. persons.

Senate amendment

The Senate amendment provides for withholding on payments of dividends, interest, and certain patronage dividends paid to individuals (and certain others) at a rate of 10 percent. Exceptions are provided for:

(1) individuals with prior year income tax of $600 or less ($1,000 on a joint return);

(2) elderly individuals with prior year income tax of $1,500 or less ($2,500 on a joint return);

(3) interest payments by electing payors of $100 or less on an annualized basis;

(4) small savings bond payments;

(5) payments by consumer cooperatives; and

(6) payments to corporations, governments, securities dealers, money market funds, exempt organizations, nominees, and certain other recipients.

Interest subject to withholding generally includes interest (including original issue discount), other than (1) interest paid by individuals, or State and local governments on tax-exempt obligations, and, (2) interest paid to nonresident alien individuals, foreign corporations and certain other foreign entities.

Dividends subject to withholding generally are distributions out of earnings and profits other than payments to nonresident alien individuals and foreign corporations.

Patronage dividends subject to withholding do not include per-unit retain allocations or patronage dividends which include consent-type qualified written notices of allocations unless 50 percent or more of such patronage dividend is paid in money or by qualified check.

In general, these provisions apply to interest and dividends paid or credited after December 31, 1982.

Conference agreement

The conference agreement generally follows the Senate amendment with clarifying and technical changes except that the effective date is July 1, 1983, instead of January 1, 1983. The conference agreement permits the Secretary to exempt certain payors from the withholding obligations for up to a 6-month period. This authority may be exercised on a case-by-case basis when the payor has attempted in good faith to comply with the withholding obligations but cannot do so without undue hardship. Under the conference agreement, this waiver of compliance with withholding obligations may apply to payments by any payor of interest, dividends, or patronage dividends.

The conferees realize that, although many elderly and low-income persons will qualify for exemption, they will need to file exemption certificates to enjoy the benefit of their exemptions. In addition, the withholding rules will affect the financial planning of many nonexempt individuals. Therefore, the Conferees anticipates that the Secretary will endeavor to inform the public about the operation of the withholding rules and the requirement that exempt individuals file exemption certificates. In this regard, the Internal Revenue Service should notify and counsel affected individuals through new or existing taxpayer-assistance mechanisms and should create forms that are as simple to understand as possible.

The conferees wish to make clear that the exemption from withholding with respect to tax-exempt obligations generally will be available if the obligation is regular on its face (e.g., in registered form if issued after December 31, 1982) and indicates that it is an obligation of a State or local government. Thus, financial institutions acting as trustee with respect to industrial development bonds would not be required to inquire whether any event has occurred that would cause the interest on the obligation to be taxable.

The exception for minimal interest payments of $100 or less on an annualized basis is modified to provide that interest payments which would not exceed $150 on an annualized basis may be exempt from withholding at the election of the payor. The conference agreement permits the Secretary to require the aggregation of payments from the same payor to the same payee.

The definition of interest is clarified, consistent with the information reporting requirements, to provide that payments by certain foreign entities and payments outside the United States by U.S. corporations whose interest payments are foreign source are not subject to withholding, except to the extent otherwise provided by regulations.

The list of exempt recipients is expanded to include simple trusts all the income beneficiaries of which are otherwise exempt individuals. Finally, the withholding credit allocation in the trust and estate context is clarified.

The conferees anticipate that the Secretary will provide for rules on the time for making deposits of withheld taxes that take into account the costs of implementing this withholding system. Specifically, the conferees anticipate that all payors of interest, dividends and patronage dividends will be permitted up to 30 calender days in which to deposit withheld amounts. This extended deposit period should apply for payments withheld during the period of July 1, 1983 to June 30, 1984. A similar extended period could apply through June 1985 for small and medium financial institutions with respect to amounts withheld on interest paid on deposits with those institutions and through June 1986 for small institutions.

2. Other compliance provisions

a. Reporting of interest

Present law

Present law contains an information reporting requirement with respect to payments of interest aggregating $10 or more to any other person during the calendar year. Any corporation that has an obligation outstanding in registered form with respect to which $10 or more of original issue discount is includible in the gross income of any holder during any calendar year must also file an information return with the Secretary. Payors of interest and persons who are required to file information returns with respect to original issue discount must also furnish information statements to recipients.

For reporting purposes. present law defines interest as including, for example, interest on any evidence of indebtedness issued by a corporation in registered form, and interest on bank deposits. In addition, the Secretary has regulatory authority to provide that interest includes interest on evidences of indebtedness issued in other than registered form by a corporation of a type offered by corporations to the public. The existing regulations do not require withholding on such obligations.

House bill

No provision.

Senate amendment

Under the Senate amendment, as under present law, every person who makes payments of interest aggregating $10 or more to any other person during the calendar year, must file an information return. In addition, any person who withholds tax from a payment of interest must file an information return with the Secretary. Under the Senate amendment, original issue discount is generally treated as paid at the time includible in income. In the case of original issue discount on a bearer obligation issued before January 1, 1983, and original issue discount which is not includible in the income of a holder periodically (including discount on short-term government obligations), the original issue discount is treated as paid on the earlier of redemption or maturity of the obligation.

Under the Senate amendment, interest subject to the information reporting requirement is defined to include interest on any obligation which is issued in registered form, or which is of a type offered to the public (other than any obligation with a maturity, at issue, of not more than 1 year which is held by a corporation); interest on bank deposits, and to the extent provided in regulations prescribed by the Secretary, any other interest (which is not specifically excluded from the definition of interest). These are generally the same categories of interest that are subject to reporting under present law except interest on all obligations in registered form or of a type offered to the public is subject to reporting rather than only interest on corporate obligations as under present law.

This provision is effective for amounts paid after December 31, 1982.

Conference agreement

The conference agreement clarifies the Senate amendment in several respects. First, the definition of interest for information reporting purposes is conformed with, and integrated into, the definition of interest for interest withholding purposes. This will simplify and conform the information reporting and withholding rules. Second, the Senate amendment is clarified by specifically providing that interest on U.S. savings obligations may (to the extent provided in regulations) be required to be reported by middlemen. Third, the definition of interest is amended to provide that interest on an obligation which is exempt from tax is not "interest" within the meaning of this provision regardless of when issued. In this connection, the conferees note that in determining whether an obligation is exempt from tax, middlemen such as financial institutions have no duty to inquire beyond the face of the obligation. Fourth, industrial loan associations are added to the list of exempt recipients for both interest reporting and withholding purposes.

As under existing law, interest on bearer obligations that is paid outside the United States by a United States person (e.g., a foreign branch of a U.S. bank) acting as a paying agent for a foreign corporate issuer (or for a U.S. corporate issuer whose interest payments are foreign-source) is exempt from the information reporting requirements, except to the extent otherwise provided by regulations. The conferees do not intend that the Secretary change his existing regulations to require reporting on such payments; however, as under present law applicable to information reporting, the Secretary continues to be empowered to require information reporting on such payments.

In contrast to present law, interest paid on bearer obligations to a United States person by a person acting as a nominee, paying agent, or other middleman is subject to the information reporting requirements if the payment is made within the United States, even if the issuer is a foreign corporation.

Finally, various technical and conforming changes are made.

b. Obligations required to be registered

Present law

Under present law, except for certain housing or energy bonds, the tax status of debt obligations is generally the same regardless of whether the obligation is issued in registered form or in bearer form.

House bill

No provision.

Senate amendment

Under the Senate amendment, the issuance of most bearer obligations by the U.S. or its agencies or instrumentalities is prohibited and certain tax benefits are denied to issuers and holders of other bearer obligations. In additon, an excise tax is imposed on bearer obligations that were required to be issued in registered form. Certain exceptions to the registration requirements are provided.

If a registration-required obligation is not issued in registered form, no interest deduction is allowable to the issuer with respect to interest (including original issue discount) paid or accrued on the obligation. In addition, the earnings and profits of a corporation issuing a registration-required obligation in bearer form will not be reduced by the amount of any interest paid or accrued on the obligation. Moreover, interest on an unregistered registration-required obligation is not exempt from tax. The Senate amendment imposes an excise tax on the issuer of a "registration-required obligation" that is not issued in registered form, equal to one percent of the principal amount of the obligation multiplied by the number of years in the term of the obligation. An exception is provided from the issuer sanctions for certain issues of bonds not intended for distribution (or redistribution in connection with the original issue) to U.S. persons.

These new registration requirements, and the associated sanctions for issuance of registration-required obligations in bearer form, will apply to obligations issued after December 31, 1982.

Conference agreement

The conference agreement generally follows the Senate amendment except that holder sanctions are imposed on U.S. persons who own bonds issued after 1982, and that were not subject to the excise tax, that should have been issued in registered form but were instead issued in bearer form. Specifically, these sanctions are the loss of capital gains treatment and the denial of loss deductions when such obligations are sold, exchanged or become worthless. The holder sanctions apply to bonds intended to be distributed outside the United States and which are excepted from the issuer sanctions, except to the extent such bonds are owned in registered form. Exceptions from the holder sanctions are provided for persons who promptly surrender bearer obligations for reissuance in registered form, for persons who hold certain bearer obligations in connection with their active conduct of a trade or business outside the United States, for securities dealers holding bearer bonds in inventory, and for persons complying with reporting requirements that may be promulgated by the Secretary, if certain conditions are satisfied in order to ensure that the bearer bonds will not be delivered to U.S. persons other than those qualifying under the exceptions.

The conference agreement also provides that the holder and issuer sanctions applicable to registration-required obligations issued in bearer form after 1982 do not apply to obligations issued in bearer form pursuant to warrants or convertible bonds issued before August 10, 1982, provided the obligations are issued under arrangements reasonably designed to ensure that they will be sold or resold only to foreign persons.

c. Returns of brokers

Present law

Under present law, every person doing business as a broker must make returns reporting on profits and losses of its customers when required under regulations issued by the Secretary. There are, currently, no regulations under this section.

House bill

No provision.

Senate amendment

The Senate amendment (1) permits the Secretary to require gross proceeds reporting, (2) requires brokers to furnish statements to their customers, and (3) clarifies the definition of broker to explicitly include persons such as dealers, barter exchanges, and other middlemen.

The bill also extends the definition of third-party recordkeepers (for administrative summons purposes) to include barter exchanges which are subject to the information reporting requirements imposed on brokers.

Generally, this provision will take effect on the day of enactment. Further, regulations must be issued under this provision within 6 months after the date of enactment; however, any such regulations may not apply to transactions occurring before January 1, 1983. The provision defining barter exchanges as third-party recordkeepers is effective for summonses served after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment.

d. Information reporting requirements for payments of remuneration for services and direct sales

Present law

Payments of remuneration

Generally, a person engaged in a trade or business must file an information return with respect to payments to another person aggregating $600 or more in the calendar year. This obligation applies to payments of wages, salaries, commissions, fees, other forms of compensation for services, and other fixed or determinable gains, profits, or income.

Direct sales

There is no reporting requirement under present law with respect to sales of consumer products for resale.

Penalties

For most types of information returns, the penalty for failure to file, or to provide statements to recipients, is $10 per failure, with a maximum aggregate penalty for each type of failure of $25,000 for any one calendar year.

House bill

No provision.

Senate amendment

Payments of remuneration

The Senate amendment adds a Code provision specifically dealing with payments of remuneration for services, effective for payments made after 1982.

Under this provision, a service-recipient (a person for whom services are performed) engaged in a trade or business who makes payments of remuneration for services performed must file an information return reporting such payments (and the name, address, and identification number of the recipient) if the remuneration paid to the person during the calendar year is $600 or more. Also, the service-recipient must furnish to the payee a statement setting forth the name, address, and identification number of the service-recipient, and the aggregate amount of payments made to the payee during the year.

Direct sales

General rule.—Unless electing the reporting rule described below, a direct seller is required to report gross purchases of consumer products for resale by any buyer purchasing $5,000 or more of such products in a calendar year (in addition to reporting commissions, etc., under the remuneration reporting requirements).

Elective requirement.—Instead of reporting gross purchases of products for resale, a direct seller may elect to report commissions and other remuneration aggregating $50 or more in the calendar year. If this election is made, the direct seller also must file a return identifying all buyers to whom aggregate sales of $600 or more are made during the calendar year.

Effective date.—The reporting requirements for direct sales apply to sales after December 31, 1983.

Penalties

Basic penalty.—A new penalty is imposed on a person who (1) fails to file a required return regarding payments for services or regarding direct sales, (2) fails to furnish a statement to the person named on the return, or (3) fails to include the entire amount required to be included on any return or statement.

The penalty is one percent for each month while the failure continues (but not to exceed five percent) of the amount required to be included on the return or statement but not so included. For failures with respect to direct sales reporting, the penalty is one-fifth of one percent per month, but not to exceed one percent of the amount not included.

Double penalty.—The penalty is doubled if failure to comply with the reporting requirements is due to intentional or reckless disregard of the law.

Minimum penalty.—The minimum penalty is $50 per failure.

Statute of limitations exception.—The Internal Revenue Service generally is prohibited from assessing this new penalty unless it is assessed, or a proceeding to collect it has begun, within six years after the last date for filing the return or statement.

Effective date.—The penalty generally applies to payments after December 31, 1982. Penalties imposed on direct sellers apply to sales made after December 31, 1983.

Conference agreement

The conference agreement follows the Senate amendment, except for deletion of the new penalty provisions and modification of the direct sales reporting requirements. Direct sellers will be required only to file information returns identifying all buyers to whom aggregate sales of $5,000 or more are made during the calendar year. No elective reporting rules are provided. The reporting requirements for direct sales will apply to sales after December 31, 1982. Penalties for failure to report remuneration paid to independent contractors or information concerning direct sales are subject to the general penalties for failure to report information. Until new regulations are issued under section 6041A, the existing regulatory exceptions under section 6041 will continue to apply. Moreover, the conferees believe that businesses should be given an adequate period of time to comply with any new requirements in such regulations.

e. Reporting of State and local income tax refunds

Present law

Under present law, the refund, credit or offset of State or local income taxes that were deducted (with a resulting tax benefit) in a prior year is includible in a taxpayer's gross income. There is no requirement that information returns with respect to such refunds be filed with the United States or that a statement regarding the refund be furnished to the recipient.

House bill

No provision.

Senate amendment

The amendment provides that an information return must be filed with the Secretary with respect to any State or local income tax refunds, credits, or offsets aggregating $10 or more paid or credited to an individual during the calendar year. In addition, a statement must be furnished to the recipient before the close of January of the calendar year following the year of refund, credit or offset.

This new requirement will apply to refunds paid, and credits or offsets allowed, after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment except that the information statements must be furnished to the individual recipients during January of the year following the year of refund, credit or offset (instead of at any time before the close of January).

f. Increased penalties for failure to file information returns and statements

Present law

Present law imposes a penalty on any person who fails to file timely information returns relating to various forms of compensation, interest, and dividends. The penalty is $10 for each such failure, but the total amount of the penalties imposed for all such failures during a calendar year cannot exceed $25,000. Persons with respect to whom information returns are filed generally are entitled to a statement of the information shown on the return. The penalty for failure to provide these statements is also $10 per failure up to $25,000 per year. Employers and plan administrators must file information returns with respect to certain deferred compensation plans. The penalty for failure to provide these returns is $10 for each day the failure continues up to $5,000. The penalty is not imposed if the failure is due to reasonable cause and not due to willful neglect.

House bill

No provision.

Senate amendment

The category of information returns subject to the general penalty for failure to timely file information returns is expanded to include broker returns and direct seller returns. The bill also increases the penalty for failure to file most information returns to $50 per failure, not to exceed $50,000 in any calendar year. When the failure to file information returns is due to intentional desregard of the filing requirements, the penalty will not be less than 10 percent of the aggregate amount of the amounts not properly reported (5 percent in the case of returns to be filed by brokers and $100 in the case of direct sellers) and the $50,000 limitation will not apply.

The provision applies to returns the due date of which (without extensions) is after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment except that (1) the penalty for failure to file information returns or statements with respect to certain deferred compensation plans (sec. 6058), and certain term, annuity and bond purchase plans (sec. 6047) is increased to $25 per day during which the failure continues, but not more than $15,000, and (2) the penalty for failure to provide information statements to taxpayers (sec. 6678) is increased from $10 per statement to $50 per statement up to $50,000 per calendar year (from $25,000). These amendments are effective for returns and statements, the due date of which (without regard to extensions) after December 31, 1982.

The conference agreement also makes certain technical and conforming amendments.

g. Increase in civil penalty on failure to supply identifying numbers

Present law

Present law imposes a penalty of $5 per failure on any person who is required by regulations (1) to include his taxpayer identification number (TIN) in any return, statement or document, (2) to furnish his TIN to another person, or (3) to include in any return or statement made with respect to another person the TIN of such other person, and who fails to comply with such requirement at the time prescribed. The penalty is not imposed if the failure is due to reasonable cause and not due to willful neglect.

House bill

No provision.

Senate amendment

The penalty for failure to supply identifying numbers is increased from $5 per failure to $50 per failure, but not to exceed $50,000 for all such failures in any calendar year. In addition, the bill provides that if any failure to include the TIN of another person in any return or statement made with respect to that other person is due to the intentional disregard of the requirements to include such other person's TIN in the return, the penalty will be $100 per failure and the $50,000 limitation will not apply.

The provision will be effective for returns the due date of which (without extensions) is after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment except that (1) the penalty for failure to include the taxpayer's own TIN in any return, statement, or document is not increased, but is kept at $5 for each such failure (instead of $50) and (2) there is no additional penalty for intentional disregard of the requirement to include another person's TIN in a return.

h. Extension of withholding to certain payments where identifying number not furnished or inaccurate

Present law

Present law imposes a penalty of $5 per failure on any person who is required by regulations (1) to include his taxpayer identification number (TIN) in any return, statement, or document, (2) to furnish his TIN to another person, or (3) to include in any return or statement made with respect to another person the TIN of such other person, and who fails to comply with such requirement at the time prescribed. The penalty is not imposed if the failure is due to reasonable cause and not due to willful neglect.

House bill

No provision.

Senate amendment

Withholding at source at a tax rate of 15 percent would be required if a taxpayer fails to supply a TIN or supplies an incorrect TIN to another person who must file certain types of information returns with respect to payments to the taxpayer. If a taxpayer fails to supply a TIN to the payor of a backup withholding payment or supplies an obviously incorrect number, then the withholding obligation rules would apply immediately. Otherwise, a 7-day grace period would apply during which the payor would not be liable if it failed to withhold, or withholds where he had an obligation to do so. The types of payments subject to this withholding requirement (back-up withholding payments) generally would include the types of payments subject to the information reporting requirements. This withholding generally would not apply to payments made to the United States or any agency or instrumentality thereof, to any State or political subdivision thereof, to any tax-exempt organization, or to any foreign government or international organization.

Except in the case of payments of compensation, etc. for which information reporting is required under section 6041 (relating to information at the source generally) or section 6041A (relating to payments to independent contractors), this requirement for withholding would apply without regard to the reporting thresholds provided for the information returns.

Generally, payment of amounts subject to this new withholding provision would be treated as wages paid by an employer to an employee and subject to the various provisions applying to collection of income tax at the source on wages.

This provision would apply to payments made after December 31, 1983.

Conference agreement

The conference agreement follows the Senate amendment except for four modifications. First, the 7-day grace period is expanded to 15 days. Second, the definition of "backup withholding payment" is clarified by defining such payment as any payment of a kind "and, to a payee" subject to information reporting. This change will assure that amounts paid to persons exempt from the information reporting requirements (and who are, therefore, also persons generally not liable to supply a TIN) are not subject to the backup withholding requirement. Third, the definition of "obviously incorrect number" is amended to apply only to numbers that contain an incorrect number of digits. Finally, the list of persons to whom backup withholding cannot apply is clarified. Thus, no backup withholding is required as to any organization exempt from taxation under section 501(a); an individual retirement plan; the United States or a State; a foreign government or international organization; a foreign central bank of issue; or to any other persons described in regulations issued by the Secretary.

i. Minimum penalty for extended failure to file

Present law

Under present law, if a taxpayer fails to file a tax return on the date prescribed therefor (including extensions) and if there is an underpayment of the tax required to be shown on such return, then he is subject to a penalty of 5 percent of the underpayment per month (or fraction thereof) while the failure continues, but not more than 25 percent. Thus, no civil penalty is imposed on the taxpayer if there is no underpayment for the year or if a refund is due. In addition, no penalty is imposed if the failure is due to reasonable cause and not due to willful neglect.

House bill

No provision.

Senate amendment

A new minimum penalty for the extended failure to file an income tax return would be imposed. If an income tax return were not filed within 60 days of the date prescribed therefor (with extensions), the penalty for failure to file would be not less than $100 even if no tax were owed. This minimum penalty would not be imposed if the failure to file the return were due to reasonable cause.

The penalty would apply to returns due after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment with the modification that the minimum penalty could not be imposed unless there was an underpayment of tax, and could not exceed the lesser of the underpayment or $100.

j. Forms of returns

Present law

In general, returns required by the tax law must be made according to the forms and regulations prescribed by the Secretary. There is no statutory or regulatory requirement that returns be filed on magnetic tape or in other machine-readable form.

House bill

No provision.

Senate amendment

The Secretary would be required to prescribe regulations providing standards for determining which returns must be filed on magnetic media or in other machine-readable form. In providing these standards, the Secretary would be directed to take into account, among all other relevant factors, the ability to the taxpayer to comply, at a reasonable cost, with such a filing requirement. In no event could the Secretary require returns of the tax imposed under subtitle A (i.e., the income tax) by individuals, estates, and trusts, to be other than on paper forms.

Conference agreement

The conference agreement follows the Senate amendment.

k. Penalty for promoting abusive tax shelters, etc.

Present law

Present law contains no penalty provision specifically directed toward promoters of abusive tax shelters and other abusive tax avoidance schemes.

House bill

No provision.

Senate amendment

A new civil penalty would be imposed on persons who organize or sell any interest in a partnership or other entity or investment, when, in connection with such organization or sale, the person makes or furnishes either (1) a statement, which the person knows is false or fraudulent as to any material matter with respect to the availability of any tax benefit said to be available by reason of participating in the investment, or (2) a gross valuation overstatement as to a matter material to the entity which is more than 400 percent of the correct value.

The penalty for promoting an abusive tax shelter is an assessable penalty equal to the greater of $1,000 or 10 percent of the gross income derived, or to be derived, from the activity.

The Secretary is given authority to waive all or part of any penalty resulting from a gross valuation overstatement upon a showing that there was a reasonable basis for the valuation and the valuation was made in good faith. This penalty is in addition to all other penalties provided for by law.

This section will take effect on the day after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment except that, (1) when a person makes or furnishes, in connection with the organization or sale of an interest in any entity or investment, a statement with respect to the availability of a tax benefit with respect to the investment, he will be liable for the penalty if he knew or had reason to know the statement was false or fraudulent as to any material matter. The addition of "has reason to know," clarifies that the Secretary may rely on objective evidence of the knowledge of a promoter or salesperson (for example) to prove that he deliberately furnished a false or fraudulent statement. For example, a salesman would ordinarily be deemed to have knowledge of the facts revealed in the sales materials which are furnished to him by the promoter. The "reason to know standard" is not, however, intended by the conferees to be used to impute knowledge to a person beyond the level of comprehension requird by his role in the transaction. Thus, this standard does not carry with it a duty of inquiry concerning the transaction.

Secondly, the term "gross valuation overstatement" is redefined to be a statement of the value of property or services which exceeds 200 percent of the correct value (instead of 400 percent).

l. Action to enjoin promoters of abusive tax shelters, etc.

Present law

Present law provides that a civil action may be brought by the United States to enjoin any person who is an income tax return preparer who engages in certain proscribed acts. Venue for such an action lies in the district in which the income tax return preparer resides or has his principal place or residence, or the taxpayer with respect to whose income tax return the action is brought resides.

House bill

No provision.

Senate amendment

The Senate amendment would permit the United States to seek injunctive relief against any person engaging in conduct subject to the penalty for organizing or selling abusive tax shelters (sec. 331 of the bill and new Code sec. 6700). Venue for these actions generally would be the district in which the promoter resides, has his principal place of business, or has engaged in the conduct subject to penalty under section 6700.

The amendment would take effect on the day after the day of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

m. Procedural rules applicable to penalties under sections 6700, 6701, and 6702

Present law

Under present law, the burden of prooof is on the Secretary in any proceeding in which the issue is whether an income tax return preparer has willfully attempted to understate the liability for tax of any person. Similarly, the burden of proof is generally on the Secretary to prove fraud. Under present law, the deficiency procedures generally apply to the collection of additions to tax, additional amounts, and nonassessable penalties.

House bill

No provision.

Senate amendment

The Senate amendment would provide for district court review of the Secretary's assessment and notice and demand of (1) the abusive tax shelters promoter penalty, (2) the civil aiding and abetting penalty, and (3) the frivolous return penalty, before the full amount of such penalties could be collected if certain procedural requirements are met.

In any proceeding involving the issue of whether any taxpayer is liable for such penalties, the burden would be on the Secretary.

The provision would take effect on the day after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

n. Penalty for substantial understatement

Present law

Under present law, penalties may be imposed on the failure to pay certain taxes shown on a return or required to be shown on a return, unless such failure is due to reasonable cause and not willful neglect. If the failure is due to negligence or fraud, additional penalties may apply.

Under present law, if a taxpayer makes a substantial property valuation overstatement which results in an underpayment of tax, then a penalty measured as a percentage of the underpayment resulting from the valuation overstatement generally is imposed without regard to fault.

House bill

No provision.

Senate amendment

A penalty of 10 percent would be imposed on any substantial understatement of income tax. For this purpose, an understatement would be the excess of the amount of income tax imposed on the taxpayer for the taxable year, over the amount of tax shown on the return. A substantial understatement of income tax would exist if the understatement for the taxable year exceeded the greater of 10 percent of the tax required to be shown on the return for the taxable year, and $5,000 ($10,000 for corporations other than subchapter S corporations and personal holding companies).

The amount of the understatement would be reduced by the portion of the understatement that is attributable to (1) the treatment of any item for which the taxpayer believed there was substantial authority, or (2) any item for which there was adequate disclosure of the relevant facts on the return. In the case of a tax shelter, the reduction would apply to the portion which the taxpayer believed was more likely than not to be the correct treatment.

A tax shelter would be defined as a transaction for which evasion or avoidance of income tax is the principal purpose.

The Secretary could waive all or a part of the penalty on a showing by the taxpayer that there was a reasonable basis for the understatement and the taxpayer acted in good faith.

The penalty would be effective with respect to returns which have a due date after 1982.

Conference agreement

The conference agreement generally follows the Senate amendment except that the application of the exceptions to the substantial understatement penalty is clarified. Under the bill, there are exceptions to the penalty based on (1) the merits of the taxpayer's filing, (2) disclosure by the taxpayer of relevant facts, or (3) waiver by the Secretary.

In a case of an item other than a tax shelter item, a taxpayer may avoid application of the substantial understatement penalty with respect to any item if (1) the treatment of the item on the return is or was supported by substantial authority or (2) all of the facts relevant to the tax treatment of the item were disclosed on the return or a statement attached to the return. Whether the taxpayer's filing position is or was supported by substantial authority will depend on the circumstances of the particular case. It will be necessary to weigh court opinions, Treasury regulations and official administrative pronouncements (such as revenue rulings and revenue procedures) that involve the same or similar circumstances and are otherwise pertinent, as well as the Congressional intent reflected in the committee reports, to determine whether the position is supported by present law and may be taken with the good faith expectation that it reflects the proper treatment of the item. The conferees did not adopt an absolute standard that a taxpayer may take a position on a return only if, in fact, the position reflects the correct treatment of the item because, in some circumstances, tax advisors may be unable to reach so definitive a conclusion. Rather, the conferees adopted a more flexible standard under which the courts may assure that taxpayers who take highly aggressive filing positions are penalized while those who endeavor in good faith to fairly self-assess are not penalized.

The standard of substantial authority was adopted, in part, because it is a new standard. The conferees are unaware of any judicial or administrative decision interpreting the phrase "substantial authority." Thus, the courts will be free to look at the purpose of this new provision in determining whether substantial authority existed for a position taken in any particular case. The conferees believe such a standard should be less stringent than a "more likely than not" standard and more stringent than a "reasonable basis" standard. Thus, it is anticipated that this new standard will require that a taxpayer have stronger support for a position than a mere "reasonable basis" (a "reasonable basis" being one that is arguable, but fairly unlikely to prevail in court upon a complete review of the relevant facts and authorities). Rather, when the relevant facts and authorities are analyzed with respect to the taxpayer's case, the weight of the authorities that support the taxpayer's position should be substantial when compared with those supporting other positions. In determining whether a position is supported by substantial authority, the courts will not be bound by the conclusions reached in law review articles, opinion letters, or private ruling on determination letters and technical advice memoranda of the Internal Revenue Service issued to or concerning a third party, but will instead examine the authorities that underlie such expressions of opinion.

The substantial understatement penalty in non-tax shelter cases also may be avoided with respect to any item if the relevent facts affecting the item's tax treatment are adequately disclosed in the return or in a statement attached to the return. Under generally applicable regulatory authority, the Commissioner may prescribe the form of such disclosure.

With respect to tax shelter items, the penalty may be avoided only if the taxpayer establishes that, in addition to having substantial authority for his position, he reasonably believed that the treatment claimed was more likely than not the proper treatment of the item. For this purpose, a tax shelter item is one that arises from a partnership or other entity, plan or arrangement the principal purpose of which is the avoidance or evasion of Federal income tax. The conferees believe that if the principal purpose of a transaction is the reduction of tax, it is not unreasonable to hold participants to a higher standard than ordinary taxpayers.

The conference agreement follows the Senate amendment in permitting the Secretary to waive the penalty with respect to any item if the taxpayer establishes reasonable cause for his treatment of the item and that he acted in good faith.

Finally, the coordination with the substantial property overvaluation penalty provision is modified so that this penalty applies only to that portion of the substantial understatement attributable to items on which the overvaluation penalty under section 6659 is not imposed.

o. Penalty for aiding and abetting the understatement of tax liability

Present law

Present law provides a criminal penalty for willfully aiding in the preparation or presentation of a false or fraudulent return, or other document under the internal revenue laws. The penalty is a fine of up to $5,000 or 3 years imprisonment, or both, together with costs. There is no comparable civil penalty on persons who aid in the preparation of false or fraudulent documents. Income tax return preparers who willfully attempt to understate the liability for tax of any person are subject to a penalty of $500 per return.

House bill

No provision.

Senate amendment

The Senate amendment would provide for a new civil penalty on any person who aids in the preparation or presentation of any portion of a return or other document under the internal revenue laws which the person knows will be used in connection with any material matter arising under the tax laws, and which the person knows will (if used) result in any understatement of the tax liability of another person.

This penalty would be $1,000 for each return or other document ($5,000 in the case of returns and documents relating to the tax of a corporation).

In general, under the Senate amendment, this penalty would be in addition to all other penalties provided by law. However, if the return preparer penalties for negligence or intentional disregard of rules or regulations, or for willful attempt to understate the tax liability of any person, could apply with respect to any document, this new penalty would not apply with respect to such document.

This provision would be effective on the day after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment with two modifications. First, the amount of the penalty with respect to documents relating to corporate tax liability is increased to $10,000 (from $5,000). Second the coordination between this penalty and the return preparer penalty is altered by allowing the Internal Revenue Service to choose which penalty it will assert if both may apply to a particular set of facts. Thus, this penalty will not apply if a return preparer penalty is actually assessed with respect to a document otherwise subject to this penalty.

p. Fraud penalty

Present law

Under present law, if any portion of an underpayment of tax is due to fraud, a civil penalty is imposed (as an addition to tax) equal to 50 percent of the entire underpayment. If part of an underpayment is attributable to negligence or intentional disregard of rules and regulations, the penalty under present law is equal to 5 percent of the entire underpayment plus 50 percent of interest payable on the portion of the underpayment attributable to negligence or disregard of rules and regulations for the period beginning on the last date prescribed for payment of the tax and ending on the date of assessment of the tax.

In the case of the windfall profit tax, both the negligence and the fraud penalty may apply to the same underpayment.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement conforms the civil fraud penalty to the negligence penalty by providing that in addition to the 50 percent fraud penalty on the entire underpayment, there is a penalty equal to 50 percent of the interest payable on the portion of the underpayment attributable to fraud for the period beginning on the last date prescribed for payment of the tax (without regard to any extension), and ending on the earlier of the date of assessment or the date of payment of the tax. Under the conference agreement, the negligence penalty does not apply in any case in which the fraud penalty has been assessed.

Finally, the conference agreement provides that when a joint return is filed, the interest addition does not apply with respect to the spouse's tax unless some part of the underpayment was due to the spouse's fraud.

The amendment applies to taxes the last day for payment of which (without regard to any extension) is after the date of enactment.

q. Frivolous returns

Present law

Under present law, a taxpayer who files a protest return, is subject to a penalty only if he or she also underpays his or her tax. Thus, if a taxpayer has paid at least the correct amount of tax through estimated tax or wage withholding, there is no penalty for filing a protest return.

House bill

No provision.

Senate amendment

The amendment would provide for an immediately assessable penalty of $500 on any individual who files a frivolous return. The penalty would apply only on documents purporting to be returns that are patently improper and not in cases involving valid disputes with the Secretary, or in cases involving purely inadvertent mathematical or clerical errors.

The deficiency procedures, under which the taxpayer would receive advance notice before the assessment, would not apply to this penalty. There would be, however, a provision allowing district court review of the assessment on payment of 15 percent of the amount assessed and the filing of a claim for refund of the amount paid.

This penalty would apply to documents filed after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment, except that the exclusion for inadvertent mathematical or clerical errors is deleted as unnecessary.

r. Criminal fines

Present law

(1) Under present law, any person and willfully attempts to evade or defeat any tax or the payment thereof is guilty of a felony and, if convicted, may be fined not more than $10,000 or imprisoned for not less than 5 years, or both.

(2) Any person who is required to pay any tax or estimated tax or keep records or report information and willfully fails to do so is guilty of a misdemeanor and is punishable by a fine of not more than $10,000 or imprisonment for not more than 1 year, or both.

(3) Any person who willfully files a false declaration under penalty of perjury, aids or assists in the preparation of a false or fraudulent document; falsely executes any document under the internal revenue laws; conceals goods, etc., to evade or defeat any tax; or does certain other acts, is guilty of a felony and upon conviction

may be fined not more than $5,000 or imprisoned for not more than 3 years, or both.

(4) Any person who willfully delivers any false or fraudulent document to the Secretary, or does certain other acts, is guilty of a misdemeanor and may be fined not more than $1,000 or imprisoned for one year, or both.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference adopted certain increases in the maximum amount of fines under the above provisions as recommended by the Department of Justice. In many cases, the maximum fine amounts had not been increased for many years and, due to inflation, no longer represented the same deterrent as was originally intended. Thus, in (1) above, the maximum penalty is increased from $10,000 to $100,000 ($500,000 for corporations); the maximum penalty amount in (2) above is increased from $10,000 to $25,000 ($100,000 for corporations); the maximum fine in (3) above is increased from $5,000 to $100,000 ($500,000 for corporations); and the maximum fines in (4) above are increased from $1,000 to $10,000 ($50,000 for corporations). The Conferees intend that, as under present law, these increased fines should continue to be treated as supplements to, and not substitutes for, imprisonment.

These increases are effective with respect to offenses committed after the date of enactment.

s. Adjustments to estimated tax provision

Present law

Under present law, an individual required to pay estimated taxes is subject to a penalty for underpayment of such taxes if he fails to pay at least 80 percent of the total amount of each installment when due. The penalty does not apply, however, if the taxpayer pays at least, (1) the tax shown on the preceding year's return (if such return was for a taxable year of 12 months); (2) pays 80 percent of the tax due by placing his income on an annualized basis; (3) pays an amount equal to 90 percent of the tax due using current year's tax rates applied to the actual income prior to the month in which the installment is paid; or (4) pays an amount equal to the tax computed using current year's rates applied to the facts and law applicable to the preceding year's return. A criminal penalty may also apply. There are no expressed exceptions to the criminal penalty.

In addition to paying estimated taxes when required, individuals are required to file declarations of estimated taxes. There is, however, no penalty for failure to file a declaration.

House bill

No provision.

Senate amendment

Under the Senate amendment, any individual or corporation that fails to make any estimated tax payment would not be subject to the criminal penalty for such failure if the civil penalty for such failure is not applicable because an exception to the civil penalty applies.

The provision would be effective on the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment. In addition, the conference agreement provides that no civil estimated tax penalty may be imposed on an individual if the individual had no tax liability for the preceding taxable year, such taxable year was a taxable year of 12 months, and the individual was a U.S. citizen or resident for the entire year.

The requirement for filing a declaration of estimated tax is terminated after 1982. Other provisions of law will, however, continue to function as if such declaration were filed. In addition, the requirement of present law that a taxpayer must pay 100 percent of each installment when due is modified to require payment only of an amount computed by taking into account the penalty provisions.

These provisions are effective for taxable years beginning after 1982.

t. Special rules with respect to certain cash

Present law

Overview

In the usual case, the Secretary may not assess and may not make notice and demand for payment of any tax unless he follows certain procedures designed to allow the taxpayer to first contest the existence and amount of the alleged deficiency. These procedures include written notice of deficiency followed by a 90-day period (150 days in the case of notices to persons outside the United States) during which the taxpayer may petition the Tax Court for review of the Secretary's determination. No assessment may be made until after this 90-day period has expired or until after a decision of the Tax Court is final. This deficiency procedure need not be followed when the Secretary reasonably believes that collection of an alleged deficiency will be jeopardized by delay. In such a case, the Secretary may declare jeopardy and immediately assess the tax, or may (in an appropriate case) terminate the taxpayer's taxable year and assess the tax due for that taxable period. The jeopardy and termination assessment procedures permit immediate assessment of an alleged tax deficiency without a preassessment notice of deficiency.

Both the jeopardy and termination assessment procedures require the Secretary to determine that there is a deficiency in tax and that the collection of this deficiency is in jeopardy. These procedures are not, therefore, well suited to cases in which the Secretary has reason to believe that a tax is owing with respect to an amount of property (for example, cash), but cannot determine the proper owner of such property.

Jeopardy assessment

If the district director believes that the assessment and collection of a deficiency in income, estate, gift or certain excise taxes will be jeopardized by delay, he may assess such deficiency and demand its immediate payment together with any interest, additional amounts and additions to tax provided for by law. The Secretary may reasonably believe that a collection of a tax is in jeopardy where, for example, the taxpayer designs to quickly depart from the United States or to conceal himself, to quickly place his property beyond the reach of the United States, or the taxpayer's financial solvency is imperiled. If after assessment, notice, and demand the taxpayer fails to pay the assessed amount, the Secretary may immediately enforce collection, subject to the right (described below) of the taxpayer to stay the enforcement proceedings by posting a bond.

Collection of the amount assessed, or any portion thereof, may be stayed by the taxpayer by filing a bond with the Secretary equal to the amount with respect to which the stay is desired. In such a case the bond must be conditioned upon the payment of the amount finally determined to be owing when due. Generally, if assessment is made and property seized for collection of the assessed amount, the property may not be sold until after the taxpayer has an opportunity for District Court review of the reasonableness of the assessment and the amount thereof, and (if applicable) the date on which a Tax Court decision is final.

Termination assessment

When the Secretary finds that the collection of income tax for the current or immediately preceding taxable year is in jeopardy because the taxpayer designs quickly to depart from the United States or to remove his property therefrom, or to conceal himself or his property, or to do any other act tending to prejudice proceedings to collect such tax, he may immediately terminate such taxable year, and assess and demand any deficiency he reasonably believes owing with respect to the taxable period terminated. A termination assessment is appropriate with respect to the income tax for the current taxable year or the preceding taxable year, but not after the due date (with extensions) of the return for the preceding taxable year. In all other situations, the jeopardy assessment provisions apply and the termination provision does not.

In the case of the current taxable year, which is terminated under the termination provision, the portion of the current taxable year starting on the first day of the current taxable year and ending on the determination date, is treated as a separate taxable year. The taxpayer's tax for the period (less any prior termination assessments) is then computed and assessed and notice and demand therefore made. Any tax collected is treated as a payment of tax for the applicable taxable year.

Judicial review of assessment

In both the jeopardy and termination assessment cases, the taxpayer is entitled to an expedited review by the Secretary, through the district director, of whether the determination of jeopardy was reasonable under the circumstances and whether the amount assessed and demanded was appropriate under the circumstances.

After review by the district director the taxpayer is also entitled to a review by the appropriate United States District Court. In the District Court, the Secretary has the burden of proving that the determination of jeopardy was reasonable under the circumstances, while the taxpayer has the burden of proof with respect to the amount assessed. This review procedure is directed only at the reasonableness of the jeopardy assessment and the amount assessed. The District Court's opinion is nonappealable, and is not a determination of the actual existence or amount of any deficiency due from the taxpayer.

In making their respective determinations, the district director and District Court may both refer to information which became available after the assessment is made.

The taxpayer is also entitled to a separate review by the District Court or Tax Court of the actual existence of any tax deficiency on which the jeopardy assessment was based.

To facilitate this review, the Commissioner must mail a notice of deficiency to the taxpayer within 60 days of the later of the due date of the taxpayer's return for the taxable year in which or for which the termination assessment was made (with extensions), or the date the taxpayer files such return. While the Secretary may terminate a taxable year more than once, he need not send out the notice of deficiency until after the close of the taxable year.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

The conference agreement adds a new provision designed to expedite jeopardy or termination assessments in cases when there is no known owner of large amounts of cash.

The current termination and jeopardy procedures are designed to address the case in which the Secretary reasonably believes, from all the circumstances, that a deficiency in tax is owing from a particular taxpayer and that the collection of such deficiency is in jeopardy. It is unclear under present law whether the jeopardy and termination procedures are available to the Secretary when cash or its equivalent cannot be associated with any particular person and the Secretary cannot, therefore, determine a deficiency in tax or its amount for an identifiable person.

The bill provides that the Secretary can presume that the collection of an amount of income tax is in jeopardy, where an individual in physical possession of more than $10,000 of cash or its equivalent denies ownership of the cash and does not claim that such cash belongs to another person the identity of whom is readily ascertainable by the Secretary (and who acknowledges ownership). In such a case, the Secretary may presume, for purposes of the jeopardy or termination assessment provisions (1) that such cash represents gross income to a single individual for the taxable year of possession taxable at 50 percent rate, and (2) that the collection of the tax on such cash would be jeopardized by delay. The Internal Revenue Service cannot assess on the same cash twice.

Notice with respect to the assessment is given to, and the right to contest the assessment is vested in, the person found in possession of the cash. However, the true owner can come forward and challenge the assessment and will be retroactively substituted for the possessor for all purposes (including establishing lien priorities) as of the date of the original assessment. In addition, the true owner will continue to have the same rights as exist under present law to recover his cash.

The terms "cash" and "cash equivalent" include cash, foreign currency, any bearer obligation and any other medium of exchange which is a type used frequently in illegal activities and specified as a cash equivalent by the Secretary in regulations. In the usual case, a cash equivalent will be valued at its fair market value, except that a bearer obligation will be deemed to have a value equal to its face amount.

This provision is effective the day after the date of enactment.

u. Special procedures for third-party summonses and third-party recordkeepers

Present law

Under present law, if an administrative summons is served on a third-party recordkeeper, then notice of the summons must also be given to the person whose records have been summoned (i.e., the taxpayer). The taxpayer can stay compliance with a third-party summons by notifying the recordkeeper in writing not to comply with the summons. To enforce the summons, the Secretary must then seek an order of a United States District Court compelling compliance.

House bill

No provision.

Senate amendment

Under the amendment, a taxpayer whose records are summoned and who wishes to prevent compliance with the summons by the recordkeeper, would be required to begin a civil action in court to quash the summons not later than the 20th day after the day notice of the summons is given. No examination of the summoned records would be allowed before the close of the 23rd day after notice were given, or, if the proceeding to quash were begun, until the court so orders. As under current law, the ultimate burden of persuasion with respect to his right to enforce the summons would remain on the Secretary.

The bill would require third-party recordkeepers to proceed to assemble summoned records upon receipt of the summons and to be prepared to produce the records on the date specified for their examination. Such recordkeepers would be entitled to reimbursement for their costs under section 7610 regardless of whether the summons is enforced.

The provisions would apply with respect to summonses initially served after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment with the clarification that when a proceeding to quash the summons is begun, the Secretary may also examine the summoned records if the taxpayer whose records are summoned consents.

v. Limitation on use of administrative summonses

Present law

Under present law, the Secretary may issue summonses for the purpose of determining liability for taxes due under the internal revenue laws unless the Internal Revenue Service has institutionally abandoned its civil tax case.

House bill

No provision.

Senate amendment

Under the amendment, the Secretary could not issue any summons or commence any action to enforce a summons if a Justice Department referral were in effect with respect to the person whose tax liability is in issue. The amendment would provide that the purposes for which an administrative summons may be issued include the right to inquire into any offense connected with the administration or enforcement of the Internal Revenue laws.

This provision would be effective the day after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

w. Withholding on pensions, annuities, and certain deferred income

Present law

Under present law, income tax generally is not required to be withheld on pension or annuity payments. However, a recipient may elect to have tax withheld on annuity payments.

House bill

No provision.

Senate amendment

The Senate amendment provides that payors generally will be required to withhold tax from all designated distributions (the taxable part of payments made from or under a pension, profit-sharing, stock bonus, or annuity plan, a deferred compensation plan where the payments are not otherwise considered wages, an IRA, or a commercial annuity contract (whether or not the contract was purchased under an employer's plan for employees)). A partial surrender of an annuity contract and certain loans from employee plans and IRAs will also be considered a distribution subject to withholding. The withholding rate is determined by the nature of the distribution. Tax will be withheld on periodic payments in excess of $5,400, under the wage withholding tables. Tax on certain total distributions will be withheld under a schedule designed to reflect the special tax treatment accorded to lump sum distributions, and tax on other non-periodic distributions will be withheld at a flat 10-percent rate. Withholding will be required with respect to payments made after December 31, 1982, unless the recipient elects not to have tax withheld.

In general, a recipient may elect (for any reason) not to have tax withheld, except that a recipient of a total distribution may elect out only to the extent that the distribution is rolled over to another eligible retirement plan. An election is generally effective for the distribution for which the election is made, except that an election with respect to periodic payments is generally effective for a calendar year. Thus, an election not to have tax withheld from periodic payments must be renewed annually.

In addition, the amendment generally requires that payors notify recipients of the withholding rules and their rights to elect out. With respect to periodic payments, notice must be provided (1) no earlier than 6 months and not later than 2 months before making the first payment, and (2) annually, within the third quarter of the calendar year. With respect to other payments, notice must be provided no later than the time of distribution.

Conference agreement

The conference agreement generally follows the Senate amendment except that (1) a recipient may elect (for any reason) not to have tax withheld from any distribution (including total distributions which are not rolled over to another eligible retirement plan); (2) an election with respect to a periodic payment is effective until revoked, although a payor would still be required to provide annual notice of a participant's right to make, renew, or revoke an election, and (3) a payor of a periodic payment is required to provide initial notice of a recipient's right to make, renew, or revoke an election no earlier than six months before and no later than the date of the first payment. It is expected that the notice will also advise recipients that penalties may be incurred under the estimated tax payment rules if the payments of estimated tax are not adequate and sufficient tax is not withheld from any designated distributions.

As under the Senate amendment, tax would generally be withheld on periodic payments pursuant to the recipient's withholding certificate. For example, a married recipient whose spouse is not a wage earner would not be subject to tax on periodic distributions payable at an annual rate of up to $7,400 if both the wage earner and his spouse were at least age 65 and a withholding certificate were filed. If no certificate is filed, the amount withheld will be determined by treating the payee as a married individual claiming three withholding exemptions. Thus, in effect, there would be no withholding on pensions payable at an annual rate of $5,400 or less.

Annuity payments and other distributions under the Civil Service Retirement System are subject to the income tax withholding rules. The conferees intend that the cost of administering the withholding rules will be borne by the Civil Service Retirement System.

The conferees recognize the difficulty some payors may have in immediately complying with the new withholding requirements for annuity payments. Accordingly, the civil and criminal penalties for failure to withhold tax will not apply to any failure before July 1, 1983, if the payor made a good faith effort to withhold, and actually withholds from any subsequent 1983 payments sufficient amounts to satisfy the pre-July 1983 requirements. No relief is provided for any failure to timely pay over any amounts that are in fact withheld. Also, the Secretary is authorized, on a case-by-case basis, to exempt payors from any obligation to withhold with respect to pre-July 1983 payments if the payor has attempted to comply in good faith, has a plan to assure its ability to comply by July 1, 1983, and cannot comply on January 1, 1983, without undue hardship. If such a waiver of the withholding obligations is granted, the payor will not be required to make up the withholding obligation out of post-June 1983 payments.

x. Pension reporting requirements

Present law

Under present law, distributions under a tax-qualified plan or annuity contract are required to be reported only if the amount includible in income totals $600 or more for the calendar year. Distributions from an IRA are required to be reported without regard to the amount of the distributions. Penalties generally apply to any person failing to file a required report.

House bill

No provision.

Senate amendment

The Senate amendment provides for reporting of necessary information by employers and plan administrators of plans from which designated distributions can be made and issuers of insurance or annuity contracts from which designated distributions can be made. The form and manner of reporting will be determined under forms or regulations prescribed by the Secretary of the Treasury. These reports are to be made to the Secretary, to the participants and beneficiaries, and to such other persons as the Secretary may prescribe. As under present law, penalties apply to any person failing to file any required report.

The provision is effective for calendar years beginning after December 31, 1982.

Conference agreement

The conference agreement generally follows the Senate amendment. In addition, the conference agreement makes it clear that an exchange of insurance contracts under which any designated distribution may be made (including a section 1035 tax-free exchange) is intended to be a reportable event even though no designated distribution occurs in the particular transaction. Thus, to insure proper reporting of any designated distributions under the new contract, it is anticipated that, under regulations to be issued by the Secretary, the issuer of the contract to be exchanged will be required to provide information to the policyholder, the issuer of the new contract, and such other persons as the Secretary may require.

y. Pension recordkeeping requirements

Present law

Under present law, no separate penalty is imposed for failure to maintain a data base sufficient to provide required reports.

House bill

No provision.

Senate amendment

The Senate amendment imposes a new penalty if the data base needed for reports is not maintained whether or not reports are due for the period during which the recordkeeping failure occurs. No penalty is imposed for a failure to meet the recordkeeping rules when the failure is due to reasonable cause and not willful neglect. Also, no penalty is imposed for a recordkeeping failure that is due to a prior failure with respect to which the penalty has already been imposed, or which occurred before 1983, if all reasonable efforts have been made to correct the prior failure. The recordkeeping penalties are effective on January 1, 1985.

Conference agreement

The conference agreement follows the Senate amendment.

z. Partial rollovers of IRAs

Present law

Under present law, distributions from qualified pension, etc., plans and IRAs are eligible for tax-free rollover treatment. However, inconsistent rules apply. For example, distributions from an IRA are eligible for tax-free rollover treatment only if the entire amount of the distribution is rolled over to another eligible retirement plan, while distributions from qualified plans are eligible for tax-free rollover treatment to the extent of any amount so transferred.

House bill

No provision.

Senate amendment

Under the Senate amendment, distributions from IRAs are eligible for tax-free rollover treatment to the extent that the distribution is rolled over to another eligible retirement plan. The provision applies to IRA distributions made after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment.

aa. Foreign investment in U.S. real property

Present law

Under legislation enacted in December of 1980, foreign investors in certain U.S. real property interests are taxable by the U.S. on the gain realized when they dispose of the interest. The provisions are enforced through complex information reporting. The legislation overrides certain nonrecognition provisions of the Code to insure U.S. taxation of the gain.

House bill

No provision.

Senate amendment

Taxation of foreign investors on disposition of U.S. real property interests would be enforced through withholding. Purchasers of U.S. real property interests from foreign owners, and certain of their agents, would be required to withhold a portion of the purchase price. Protections against liability are provided so that withholding would apply only if the purchaser or his agent had actual knowledge or had received formal notice that the seller was foreign. Agents for the transferor would have to withhold if they had knowledge, reason to believe, or notice, and failed to notify the transferee. Withholding would not apply to a purchaser buying a principal residence for $200,000 or less, or to sale of stock on an established U.S. market. The Secretary could reduce or eliminate withholding on request in certain other cases. The Secretary is authorized to remove current reporting obligations that are not needed because of withholding.

The provision would impose withholding for amounts paid on or after 30 days after enactment.

Conference agreement

The conference agreement does not include the Senate amendment.

bb. Returns with respect to foreign personal holding companies

Present law

Certain information returns are required of officers, directors, and 50-percent U.S. shareholders of companies that are FPHC's at year's end. Some return requirements overlap. Moreover, staggered filing dates may cause repetitive paperwork. There is no civil penalty for failure to file.

House bill

No provision.

Senate amendment

The Commissioner would be given flexibility in setting due dates and waiving duplicate filings for foreign personal holding company reports and returns. The amendment also makes changes in reporting requirements.

A $1,000 civil penalty for failure to file a proper return would be imposed.

The provision would apply to taxable years of foreign corporations beginning after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

cc. Penalty for failure to furnish information returns with respect to certain foreign corporations; reporting requirement for corporations controlled by foreign persons

Present law

When a taxpayer fails to furnish adequate information about a foreign corporation he controls, he is subject to a penalty reducing the relevant foreign tax credit by 10 percent. Additional penalties of five percent of the credit accrue quarterly on continuing failure. There is no specific statutory reporting requirement for a U.S. corporation (or a foreign corporation operating in the United States) that is controlled by a foreign person and that enters into transactions with related parties.

House bill

No provision.

Senate amendment

The Senate amendment supplements the existing penalty by adding an alternative flat penalty of $1,000 per tax year for which failure exists. Ninety days after notification of failure, additional $1,000 penalties accrue every 30 days, up to a $24,000 maximum. Amounts paid under the flat $1,000 penalty reduce amounts due under the existing penalty reducing the foreign tax credit. This provision applies to annual accounting periods ending after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment, but adds a new reporting requirement for certain foreign-controlled corporations. In general, these requirements apply both to U.S. corporations and to foreign corporations engaged in trade or business in the United States ("reporting corporations"), but only if they are controlled by a foreign person (defined to include certain possessions residents). This control test requires reporting if at any time during a taxable year a foreign person owns 50 percent or more of the stock of the reporting corporation (either by value or by voting power).

The reporting corporation must furnish certain information about any corporation that (1) is a member of the same "controlled group" as the reporting corporation (a group that generally includes brother-sister corporations as well as the reporting corporation's parent and subsidiaries), and that (2) has any transaction with the reporting corporation during the taxable year. The information that the reporting company is to report is such information as the Secretary may require that relates to the related company's name, its principal place of business, the nature of its business, the country in which it is organized and in which it is resident, its relationship with the reporting corporation, and its transactions with the reporting corporation during the year.

The conference agreement imposes penalties for violation of this new reporting requirement that are similar to the Senate amendment's new supplemental penalties for failure to supply information under the existing reporting requirement (relating to controlled foreign corporations). Reasonable cause, as shown to the satisfaction of the Secretary, precludes imposition of this penalty.

This new reporting requirement applies to taxable years beginning after December 31, 1982.

dd. Access to records and persons not found in the United States

Present law

Documents held abroad.—The Code specifically confers jurisdiction to enforce an administrative summons only when a U.S. citizen or resident resides or is found in a U.S. judicial district. There is generally no procedure to require timely production of documents held abroad. The Commissioner may issue summonses to examine any books, papers, records, or other data that may be relevant or material to a tax inquiry. To enforce an administrative summons, the Commissioner must show that (1) the investigation will be conducted pursuant to a legitimate purpose, (2) the inquiry may be relevant to that purpose, (3) the information sought is not already within his possession, and (4) the administrative steps required by the Code have been followed. To the extent that a summons is overbroad it is invalid, because to that extent, the inquiry is irrelevant to a legitimate purpose. In addition, the Secretary must at all times use the summons authority in good faith.

Treaty benefits.—The Internal Revenue Code generally imposes a 30 percent tax on the gross amount of certain passive income which arises from U.S. sources and is paid to foreign persons. The 30 percent tax on such gross amounts is collected by withholding at the source. The person required to withhold the tax (the "withholding agent") may be the actual payor of the income or certain agents of the payor, such as banks or other financial intermediaries, which have control over, or custody of, such income.

Tax treaties between the United States and other countries commonly provide, on a reciprocal basis, for reduced rates or elimination of U.S. tax on various categories of passive income paid to residents of such other countries. Generally, under current regulations, a foreign recipient of U.S. source passive income may obtain a reduction or elimination of U.S. tax on such income under an applicable treaty if the recipient provides the payor or other person having control of such income with a completed Internal Revenue Service Form 1001. The Form 1001 identifies the owner of the income, states the character of the income, and contains a statement that the recipient qualifies for the relevant treaty benefits. Regulations prescribe a different method, the "address method," for obtaining reduced rates of withholding tax for U.S. source dividends paid to foreign persons which is different from the Form 1001 procedure that applies to other types of passive income. Under the address method, a recipient of U.S. source dividends who has an address in a country with which the United States has a tax treaty will, with limited exceptions, be presumed to be a resident of such country for purposes of obtaining reduced rates of tax on dividends under the treaty. The pertinent regulations provide that the withholding agent may withhold on dividends at the reduced treaty rates in reliance upon the foreign address of the recipient unless the agent has knowledge that the recipient is not a resident of the country under whose treaty the reduced rates are claimed.

House bill

No provision.

Senate amendment

The Senate amendment extends the jurisdiction and the summons power of the United States District Court of the District of Columbia to reach U.S. citizens and residents not present in the United States.

Conference agreement

Documents held abroad.—The Conference agreement generally follows the Senate amendment, but adds certain provisions. The agreement adds a formal document request procedure that is intended to discourage taxpayers from delaying or refusing disclosure of certain foreign based information to the Internal Revenue Service.

The Conference agreement provides that if a taxpayer fails to "substantially comply" with a "formal document request" arising out of the tax treatment of any item, upon motion of the Secretary, any court having jurisdiction over a civil proceeding in which the tax treatment of the examined item is at issue shall prohibit the introduction into evidence by the taxpayer of any "foreign-based documentation" covered by such request, unless such documentation was provided to the Secretary within 90 days, or a later date to be set by the Secretary, of the mailing of the request.

Whether a taxpayer has substantially complied with a formal document request will depend on all the facts and circumstances. For instance, if the Internal Revenue Service presents a taxpayer with a formal document request for 10 items and the taxpayer produces 9 of them but fails (without reasonable cause) to produce the one requested document that appears to a court to be the most significant item, a court may decide that there has not been substantial compliance and exclude all of the items. However, when the Service issues multiple requests in the course of an audit, and when, for example, the taxpayer fails to comply with one particular request for only one document, the taxpayer's timely satisfaction of other requests is one factor (but not the only factor) to be considered in determining whether his overall compliance has been substantial. If overall compliance in such a situation has been substantial, the document requested but not supplied could be admissible.

The term "foreign-based documentation" means any documentation which is outside the United States and which may be relevant or material to the tax treatment of an examined item. It includes documents held by a foreign entity whether or not controlled by the taxpayer. The term "documentation" includes, but is not limited to, books and records.

The term "formal document request" means any request (made in the course of an audit and after the normal request procedures have failed to produce the requested documentation) for the production of foreign-based documentation which is mailed by registered or certified mail to the taxpayer at his last known address and which sets forth the time and place for the production of the documentation, a statement of the reason the documentation previously produced (if any) is not sufficient, a description of the documentation being sought, and the consequences to the taxpayer of the failure to produce the documentation. The normal request procedures that a formal document request must follow include an information document request. The conferees do not intend that the formal document request procedure will be used as the routine beginning of an examination. The conferees intend that the Commissioner establish procedures for administrative review of proposed formal document requests before issuance. The Service can require in its request that foreign documents be translated into English.

The sanction of nonadmissibility does not arise if the taxpayer establishes that the failure to provide the documentation as requested by the Secretary is due to reasonable cause. In determining whether there was reasonable cause for failure to produce, a court may take into account whether the request is reasonable in scope, whether the requested documents or copies thereof are available within the United States, and the reasonableness of the requested place of production within the United States.

The fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the requested documentation is not reasonable cause. Frequently, taxpayers choose to operate through a particular country because of its restrictive nondisclosure laws. Even so, the amendment's preclusion of the use of foreign nondisclosure law as a defense is narrow in scope. The only effect of the preclusion is that the taxpayer cannot introduce at trial records that he allegedly could not earlier produce on audit.

The conferees recognize that minority status can prevent a taxpayer from being able to produce certain records held by a foreign entity. However, the conferees also recognize that taxpayers may seek to hide behind minority status to avoid production of records. Accordingly, a determination of whether minority status is reasonable cause will be determined by the facts and circumstances of the case.

Reasonable cause may excuse delay in production. For example, a requirement of translation of documents into English may not be reasonably possible in 90 days.

The conference agreement provides for judicial review of a formal document request at the time served. Any person to whom a formal document request is mailed has the right to begin a proceeding to quash that request not later than the 90th day after the day such request was mailed. In this proceeding, the taxpayer may contend, for example, that all or part of the documentation requested is not relevant to the tax issue, that the place of requested production within the United States is unreasonable, that the requested documents or copies thereof are available within the United States, or that there is reasonable cause for failure to produce or delay in production.

The reasonableness of a demand for the production of the originals of foreign documents rather than copies may be resolved in judicial proceedings to quash the request. If the foreign country makes it impossible to remove the original documents requested, not because of secrecy laws but, for example, because of foreign tax laws or laws as to the rights of creditors, true copies may be sufficient.

In any proceeding to quash, the Secretary may seek to compel compliance with the request. Jurisdiction over a proceeding to quash is retained in the United States District Court for the district in which the person to whom the formal document request is mailed resides or is found. If that person resides and is found outside the United States, the United States District Court for the District of Columbia has jurisdiction.

In a proceeding to quash, as under the current rules for administrative summonses, the Commissioner has the burden of showing relevance and materiality of the requested records. In addition, the Commissioner must show that the investigation will be conducted pursuant to a legitimate purpose, that the information sought is not already within his possession, and that the administrative steps required by the Code have been followed. During the proceeding, the running of the 90-day period for compliance with a formal document request is suspended. If the district court rules against the taxpayer, the taxpayer may appeal the court's order immediately.

The taxpayer generally has 90 days from the day of mailing to comply with a formal document request. However, the Secretary or a court having jurisdiction over a motion to quash the request may extend the period. The court may extend the period in response to a motion to quash or in response to a motion to extend the period that is not part of a motion to quash. For example, a court could find that a taxpayer had reasonable cause for failure to produce an item within 90 days and set a later date for production.

Treaty benefits.—In addition, the conference agreement would require the Secretary to establish procedures to limit treaty benefits to those persons who are justifiably entitled to such benefits. The problem is particularly acute because of the large number of income tax treaties with low tax bank secrecy jurisdictions. Congress has repeatedly shown its concern about the vulnerability of the treaty system to manipulation. In June of this year, the Subcommittee on Commerce, Consumer, and Monetary Affairs of the House Government Operations Committee held a hearing on the use of foreign addresses by U.S. individuals to evade tax by posing as non-resident aliens. The Subcommittee on Oversight of the House Committee on Ways and Means held hearings in April 1980 about abuses of income tax treaties and in April 1979 about the abuse of offshore tax havens. These hearings have demonstrated that substantial amounts of passive income, which would be tax-free in the hands of foreigners, finds its way into the hands of U.S. persons and residents of nontreaty countries who should be paying tax on it. They have also shown concern about the use of treaties by those not justifiably entitled to their benefits (so-called "treaty shopping").

The Internal Revenue Service and Treasury believe that the current procedures are insufficient for insuring that U.S. persons do not pose as foreigners entitled to tax treaty benefits and that foreigners do not take advantage of treaties of countries of which they are not resident. The conferees share the concerns regarding the improper obtaining of treaty benefits and agree that the current procedures are insufficient. The address system of withholding of tax on U.S. source dividends is particularly vulnerable to abuse. The Form 1001 filing procedure which applies to income other than dividends is similarly subject to abuse in that it requires a person claiming treaty benefits only to submit an unverified, self-serving statement to a withholding agent, who is entitled to rely on such statement for purposes of reducing the amount of tax withheld.

A number of alternatives to the present enforcement system exist, including the adoption of a refund system of withholding tax on passive income. A refund system would require withholding agents to withhold U.S. tax at the statutory 30 percent rate on all U.S. source passive income paid to foreign persons, regardless of the potential application of a treaty provision reducing the 30 percent rate or eliminating the tax altogether. The foreign recipient who claims treaty benefits would then be required to file a claim for a refund on an annual tax return. Supportive documentation would be required.

Another approach, the "certification system," would require the foreign recipient to file a certificate of residence from the competent authority of the country whose treaty benefits are being sought.

The conference agreement requires the Secretary to consider the refund system and the certification system as methods of limiting treaty benefits to those persons entitled to them. The Secretary is not limited to consideration of these methods; he should consider other methods as well. In developing such procedures to prevent abuse the Secretary should consider the extent to which any procedures would prevent abuse, the administrability of such procedures (including the ability of U.S. treaty partners to provide cooperation), any negative effect on investment in the U.S. by foreign persons which could be caused by increased costs of complying with the procedures, and the effect on U.S. investment abroad should U.S. treaty partners apply a similar method to that utilized by the United States.

The provisions would require the Secretary to establish procedures, as described above, within two years of the date of enactment.

ee. Authority to delay date for filing certain returns relating to foreign corporations and trusts

Present Law

Acquisition of a 5-percent interest (or an additional 5-percent interest) in a foreign corporation or the creation of or transfer of property to a foreign trust causes a U.S. person to have to file an information return. Beginning service as an officer or director of a foreign corporation creates a similar requirement. The returns are due 90 days after the triggering events.

House bill

No provision.

Senate amendment

The Commissioner would be given flexibility to delay the date for reporting of certain transactions relating to foreign corporations and foreign trusts beyond the current due date.

The provision would apply to returns filed after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

ff. Technical amendment to section 905(c)

Present law

The last sentence of section 905(c) appears to provide that interest on a U.S. tax underpayment triggered by a refund of foreign taxes begins to run before receipt of the refund. Other Code provisions begin the running of interest on receipt of the refund and provide a penalty for failure to report a refund.

House bill

No provision.

Senate amendment

The last sentence of section 905(c) would be eliminated. This provision would be effective for all years.

Conference agreement

The conference agreement follows the Senate amendment.

gg. Daily compounding of interest

Present law

Under present law, interest payable to or by the United States under the internal revenue laws is not compounded.

House bill

No provision.

Senate amendment

All interest payable under the internal revenue laws would be compounded daily. The change would also affect any other amounts computed by reference to the interest rate provided for in the Code.

This compounding requirement would apply to interest accruing after December 31, 1982, on amounts (including interest) remaining unpaid after that date.

Conference agreement

The Conference agreement follows the Senate amendment except that daily compounding is not required for purposes of the penalties on failure to pay estimated taxes. In a case in which the principal portion of an obligation is satisfied, and interest remains outstanding, such interest will, of course, be compounded.

hh. Semi-annual determination of rate of interest

Present law

Under present law, the rate of interest paid on underpayments, overpayments, and for certain other purposes under the internal revenue laws is determined once a year based on September's average predominant prime rate.

House bill

No provision.

Senate amendment

Under the amendment, interest rates would be redetermined twice a year on the basis of the average adjusted prime rate charged by commercial banks during the six-month period ending September 30 (effective January 1 of the succeeding calendar year), and March 31 (effective July 1 of the same calendar year).

The amendment would be effective for adjustments taking effect after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment.

ii. Restrictions on payment of interest for certain periods

Present law

In general, under present law, interest on refunds, credits, and offsets runs from the date of overpayment or (in the case of a credit) to the due date of the amount against which the credit is taken. An overpayment resulting from a net operating loss carryback, net capital loss carryback, or credit carryback is treated as having occurred at the close of the year in which the carryback arose.

In the case of an underpayment of tax, interest runs from the last date prescribed for payment of the tax without regard to extensions, to the date the tax is paid. If there is an underpayment of tax for any taxable year, and the amount of the underpayment is reduced by reason of the carryback of a net operating loss, net capital loss, or because of the increase in any credit for the taxable year because of a credit carryback from another taxable year, such reduction is not effective for any period prior to the last day of the taxable year in which the net operating loss, the net capital loss, or credit carryback arises.

House bill

No provision.

Senate amendment

Under the Senate amendment, the general rule with respect to the payment of interest on overpayments is unchanged when the credit or refund is claimed in a timely filed return. However, when the return is late because it is filed after the due date (determined with regard to extensions) no interest is payable on the overpayment for any period prior to the date on which the return is filed. For this purpose, and for purposes of determining whether a refund has been made within 45 days after the return is filed, no return is treated as filed until filed in processible form.

Under the Senate amendment, an overpayment due to a net operating loss or a net capital loss carryback, or a credit carryback is deemed not to arise before the application for tentative carryback adjustment is made, or the claim for credit or refund is filed with respect to such overpayment.

Conference agreement

Due to considerations relating to the treatment of offsets (for example, in audit situations) the conferees decided to revise the provisions of the Senate amendment dealing with restrictions on payments of interest on certain refunds. Under the agreement an overpayment resulting from a net operating loss carryback, a net capital loss carryback, or credit carryback would be treated as having occurred on the due date (without extensions) of the return for the year in which the carryback arose. In the case of a refund, the return for the loss year would be treated as not filed prior to the time the claim for refund therefor is filed. Under the conference agreement, no interest would be paid on a refund claimed on a late return if the refund is made within 90 days after the return is filed.

Conforming amendments would be made in the rules relating to interest on underpayments.

Under the bill, for purposes of the payment of interest on overpayments, a return would not be treated as filed until it is filed in processible form.

The provisions regarding late returns and processible returns would be effective for returns filed after the 30th day after the date of enactment. The provision regarding interest overpayments due to carrybacks would be applicable to interest accruing 30 days after enactment.

jj. Disallowing deductions for drug dealing

Present law

Ordinary and necessary trade or business expenses are generally deductible in computing taxable income. The Code makes certain otherwise ordinary and necessary expenses incurred in a trade or business nondeductible in computing taxable income. These nondeductible expenses include fines, illegal bribes and kickbacks, and certain other illegal payments.

House bill

No provision.

Senate amendment

All deductions and credits for amounts paid or incurred in the illegal trafficking in drugs listed in the Controlled Substances Act would be disallowed.

This provision would be effective for amounts paid or incurred after the date of enactment in taxable years ending after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

kk. Internal Revenue Service staff increases

Present law

Public Law 97-92 enables the Internal Revenue Service to maintain an average of 85,363 positions during fiscal year 1982. The Administration's budget request for fiscal year 1983 includes a net increase in Internal Revenue Service manpower of 3,310 average positions.

House bill

No provision.

Senate amendment

The Senate amendment contains a sense of the Congress resolution that additional funds be appropriated to the Internal Revenue Service pursuant to the Administration's request for fiscal year 1983 and that additional funds be provided in future years for the Internal Revenue Service sufficient to collect additional tax revenues of at least $1 billion in fiscal year 1984 and $2 billion in fiscal year 1985.

Conference agreement

The conference agreement follows the Senate amendment.

ll. Reports on forms

Present law

No provision.

House bill

No provision.

Senate amendment

The Secretary is required to study and report to Congress, no later than June 30, 1983, on methods of modifying the design of the forms used by the Internal Revenue Service to achieve greater accuracy in the reporting of income and the matching of information reports and returns with the actual income tax returns.

Conference agreement

The conference agreement follows the Senate amendment.

3. Tax treatment of partnership items

Present law

For income tax purposes, partnerships are not taxable entities. Instead, a partnership is a conduit, in which the items of partnership income, deduction, and credit are allocated among the partners for inclusion in their respective income tax returns.

Partnerships are required to file an annual information return setting forth the partnership income, deductions, and credits, names and addresses of the partners, each partner's distributive share of these items, and certain other information required by the regulations. A penalty is imposed on the partnership for each month (not to exceed 5 months), that a partnership return is late or incomplete. The amount of penalty for each month is $50 multiplied by the total number of partners in the partnership during the partnership's taxable year.

Since a partnership is a conduit rather than a taxable entity, adjustments in tax liability may not be made at the partnership level. Rather, adjustments are made to each partner's income tax return at the time that return is audited. A settlement agreed to by one partner with the Internal Revenue Service is not binding on any other partner or on the Service in dealing with other partners. Similarly, a judicial determination of an issue relating to a partnership item generally is conclusive only as to those partners who are parties to the proceeding.

The Code provides a period of limitations during which the IRS can assess a tax or a taxpayer may file a claim for refund. Generally, the period is 3 years from the date the tax return is filed (if filed before the due date, the due date is treated as the date filed). If more than 25 percent of the gross income is omitted from a return, the statutory period for assessment is 6 years. In the case of a partnership, the income tax return of each of the partners begins that individual partner's period of limitations. Except in the case of Federally registered partnerships, the date of filing of the partnership return does not affect the individual partner's period of limitations. In order to extend the period of limitations with respect to partnership items, the IRS is required to obtain a consent for extension of the statute of limitations from each of the partners—not the partnership. Generally, an agreement to extend the period of limitations relates to all items on the return of the partner who consented to the extension.

The application of the partnership return filing requirement to certain foreign based partnerships with U.S. partners is unclear. There is no express requirement that a U.S. person report the acquisition or disposition of an interest in a foreign partnership.

Windfall profit tax.—Under present law, taxable crude oil which would otherwise be treated as produced by a partnership, is allocated among the partners of the partnership according to their income interest. Each partner to whom crude oil is allocated under this rule is treated as the producer of such crude oil. Since each partner is treated as the producer of an allocable share of the partnership's production of crude oil, the partnership must report sufficient details to permit their partners to compute their allocable share of the windfall profit tax on partnership's crude oil production. In addition, each partner generally will certify his status to the partnership when such status is relevant to any special tax treatment, such as lower rates for independent producers or an exemption based upon the identity of the producer, so that first purchasers can compute the proper withholding of windfall profit taxes.

House bill

No provision.

Senate amendment

The Senate amendment contains a number of provisions designed to promote increased compliance and more efficient administration of the tax laws.

Conference agreement

a. In general

Under the conference agreement, the tax treatment of items of partnership income, loss, deductions, and credits will be determined at the partnership level in a unified partnership proceeding rather than in separate proceedings with the partners.

Except as otherwise provided in subchapter C of Chapter 63 as added by the conference agreement, the tax treatment of any partnership item is to be determined at the partnership level. New rules are adopted which govern the determination of the treatment of partnership items and resulting adjustments, both at the administrative and judicial levels.

b. Administrative proceedings

Consistency requirement

Under the conference agreement, each partner is required to treat partnership items on his return consistently with the treatment on the partnership return. Where treatment is, or may be, inconsistent (or no partnership return is filed), the consistency requirement is waived if a statement is filed by the partner identifying the inconsistency. Similarly, the consistency requirement may be waived at the partner's election if the partner establishes to the satisfaction of the Secretary that the return treatment of an item was consistent with an incorrect schedule furnished the partner by the partnership.

Failure to satisfy the consistency requirement, if not waived, will result in an adjustment to conform the treatment of the item by the partner with its treatment on the partnership return. Any additional tax resulting from such computational adjustment will be assessed without either the commencement of a partnership proceeding or notification to the partner that the inconsistent item will be treated as a nonpartnership item.

Notice requirements

Each partner whose name and address is furnished to the Secretary will receive notice of the commencement of a partnership level audit as well as notice of the final partnership administrative adjustment (FPAA), provided sufficient information is furnished to the Secretary (at least 30 days before any such notice is mailed to the tax matters partner) to enable the Secretary to determine that the partner is entitled to the notice. An exception to the notice requirement is made for anyone with a less than one-percent interest in the profits of a partnership with more than 100 partners. However, a group having an interest in the aggregate of 5 percent or more in partnership profits may designate a member of the group as a notice partner to receive notice on behalf of the group. Otherwise, the notice furnished the tax matters partner (TMP) is treated as notice to these small partners.

In providing notices, the Secretary may use the names, addresses, and profits interests shown on the partnership return or may use other information furnished by the TMP or other person pursuant to regulations.

The TMP is the general partner so designated pursuant to regulations or, in the absence of such designation, the partner with the largest profits interest in the partnership at the end of the year involved (in the event there are several partners so qualifying, the one whose name would appear first in an alphabetical listing is selected). Otherwise, the TMP will be selected by the Secretary. Since the identity of the TMP may not be known to the Secretary, mailing of any notice in care of the tax matters partner at the address where the partnership business is carried on will constitute mailing of the notice for purposes of determining whether other requirements imposed on the Secretary are complied with or whether any action, such as mailing notices to other partners, is timely taken.

If the information furnished the Secretary is sufficient, the names, addresses, and profits interests of persons with profits interests in the partnership through one or more pass-through partners will be used with respect to such profits interests in lieu of the names, addresses, and profits interests of the pass-through partners.

Notice partners are entitled to have notice of the partnership proceeding mailed to them at least 120 days before the notice of the FPAA is mailed to the TMP and to have the notice of the FPAA mailed to them not later than 60 days after such notice is mailed to the TMP. Notice partners for this purpose include partners with a less than one-percent interest in profits (in partnerships with over 100 partners), and the notice requirement as to such partners is satisfied by notice to the TMP, or if such partner is a member of a 5-percent or greater group, by notice to the designated member of such group.

Late notification

If, when notice of the proceeding is mailed to any partner, the period within which to commence a judicial proceeding to redetermine the FPAA has expired without commencement of such a proceeding, or if any court decision has became final, the partner may elect to have such determination, such court decision, or a settlement agreement entered into with another partner with respect to the same partnership year apply. If the partner does not so elect, all partnership items will be treated as nonpartnership items in determining his liability. If administrative or judicial proceedings have not terminated but the notice of the proceeding is untimely, the partner will be a party to the proceedings unless he elects to have the terms of a settlement with any other partner applied to him or to have all partnership items treated as nonpartnership items.

Other notice requirements

Only one notice of FPAA may be mailed to a partner for any one year of a partnership in the absence of fraud, malfeasance, or a misrepresentation of a material fact.

To the extent provided in regulations, the TMP will be required to keep partners informed of all administrative and judicial proceedings. Notices received by pass-through partners must be forwarded within 30 days to persons holding an interest in partnership profits or losses through the pass-through partner. The responsibility for forwarding such notices is on the TMP of any pass-through partner which is itself a partnership. It is intended that no obligation will be imposed on the TMP with respect to partners wishing to be informed about routine or minor events.

All partners have a right to participate in the partnership proceeding but may waive such rights and any restrictions, such as a restriction on assessment, on the Secretary. The place and time of meetings and other events involving the Internal Revenue Service will be determined by Service representatives and the TMP.

Settlements

Settlement agreements in the absence of fraud, are binding on the Secretary and partners participating in the settlement, except as the settlement may otherwise provide. Indirect partners, unless properly identified as required by the statute, will be bound by settlements entered into by the pass-through partner. The Secretary must offer to any partner who so requests settlement terms that are consistent with the settlement with any other partner. Except where notice to a partner of the proceeding was not timely, a request for such settlement terms must be made, with respect to any settlement entered into before mailing a notice of FPAA to the TMP, before the expiration of 150 days after such mailing.

The TMP may enter into a settlement on behalf of, and binding upon, less than one-percent profits partners, in partnerships with over 100 partners, who are not members of a notice group. However, any such partner may file a statement within the time prescribed by the Secretary providing that the TMP does not have authority to settle on behalf of such partner. No partner other than the TMP (and other than a pass-through partner with respect to indirect partners) may bind any other partner with respect to a settlement agreement.

Assessment of tax

Any deficiency resulting from an administrative determination generally may not be assessed until 150 days after mailing the notice of FPAA to the TMP, or if within the 150-day period a Tax Court proceeding is commenced, until the decision in such proceeding has become final. Any action to assess or collect the tax in violation of this restriction may be enjoined in the proper court.

If a timely court proceeding is not commenced, the deficiency assessed against any partner with respect to partnership items affected by a FPAA may not exceed the amount determined in accordance with such adjustment.

c. Judicial review of FPAA

Commencement of action

The TMP, within 90 days after the mailing of the notice of FPAA, may file a petition for readjustment of partnership items in the Tax Court, the district court of the United States for the district in which the partnership's principal place of business is located, or the Claims Court. During such 90-day period, no other partner may file a petition for judicial review.

If the TMP does not file a petition, any notice partner or 5-percent group with an interest in the outcome may within 60 days following such 90-day period, file a petition with any of the courts in which the TMP may file a petition. Only one proceeding may go forward. The first action filed in the Tax Courts will establish jurisdiction or, if no petition is filed with the Tax Court, the first action filed in either of the other courts will go forward. Other actions will be dismissed. The TMP may intervene in an action brought by another partner.

Right to participate

Each partner with an interest in the outcome shall be treated as a party to the action and will be allowed by the court to participate in the action. A partner does not have an interest in the outcome after partnership items as to such partner become nonpartnership items (under sec. 6231(b)), or the period for assessment with respect to partnership items of such partner has expired.

Deposit requirement where action in district court or Claims Court

As a condition to filing a petition in either the appropriate district court or the Claims Court, the partner filing the petition (including each member of a 5-percent group which files a petition) must deposit with the Secretary the amount by which such partner's tax liability would be increased if treatment of partnership items on the partner's return were made consistent with the partnership return as adjusted by the FPAA. The court may by order determine that this jurisdictional requirement is satisfied if a good faith effort to comply was made and any shortfall in the amount required to be deposited is timely corrected.

The amount required to be deposited will be refunded upon request of the depositing partner if jurisdiction to proceed is established in the Tax Court. "However, if, upon expiration of the 150 day filing period, no Tax Court petition is filed, the Secretary may assess any deficiency of the depositing partner resulting from the FPAA and apply such deficiency against the deposited amount. Likewise, the Secretary may assess and collect any deficiencies of other partners resulting for the FPAA if jurisdiction is established in the District Court or Claims Court pending a decision on the merits."

Any amount required to be deposited shall, while deposited, be treated as a payment of tax only for purposes of Chapter 67, relating to interest.

Scope of judicial review

The court acquiring jurisdiction of a partnership proceeding shall have jurisdiction to determine all partnership items of the partnership taxable year to which the FPAA relates and the proper allocation of such items among the partners. The court's decision has the effect of a final decision of the Tax Court or a final judgment or decree and will be reviewable if review is sought by the TMP, a notice partner, or a 5-percent group.

Dismissal of an action other than a dismissal for lack of jurisdiction, shall be considered a decision that the FPAA is correct.

d. Request for administrative adjustment

General rule

A partner may file a request for administrative adjustment (RAA) of partnership items for a partnership taxable year within 3 years after the partnership return was filed (or, if later, the last day for filing such return, determined without extension) and before the mailing of a notice of FPAA to the TMP for such taxable year.

Request by TMP on behalf of the partnership

An RAA, filed by the TMP, may serve as an amended return correcting the treatment of items on the original partnership return, in which case the Secretary may treat the changes made as corrections of clerical or mathematical errors on the original return.

In other cases, an RAA generally serves as a claim for refund. In such cases, when the RAA is filed by the TMP, the Secretary may (i) make all refunds and credits to all partners resulting from the requested adjustments provided the adjusted items continue to be partnership items with respect to any partner, or (ii) commence a partnership proceeding.

The RAA filed by the TMP must show the effect of the requested adjustments on the distributive shares of the partners and other information as required by regulations.

Other requests

Each partner may file an RAA on his own behalf. In such case, the Secretary may (i) process the request in the same manner as a claim for refund relating to nonpartnership items, (ii) assess any tax resulting from the requested adjustments, (iii) notify the partner that all items to which the request relates will be treated as nonpartnership items, or (iv) commence a partnership proceeding.

Judicial review by TMP on behalf of the partnership

The TMP may file a petition for review in the Tax Court, the appropriate district court, or the Claims Court after the expiration of 6 months from the date of filing the RAA and within 2 years of such filing, with respect to any part of the requested adjustment not allowed. Such a petition may not be filed after a notice of the commencement of a partnership proceeding is mailed to the partnership. If, when such notice is mailed, the 2-year period within which a petition could have been filed has not expired and the Secretary fails to mail timely notice of a FPAA, the TMP shall have 6 months after the expiration of the period in section 6229(a) within which to file a petition. The TMP and the Secretary may agree to extend the 2-year period for filing a petition.

In any event, no petition for review with respect to an RAA may be filed after a timely notice of FPAA has been mailed by the Secretary. If the petition has been filed when a timely notice of FPAA is mailed, the proceeding will be treated as a proceeding with respect to the FPAA, except that no deposit will be required to establish jurisdiction in the appropriate district court or the Claims Court.

Other partners are to be treated as parties to any action brought by the TMP with respect to unallowed adjustments requested in an RAA under rules similar to those applicable when a petition is filed to review a FPAA.

Judicial review of an RAA filed by the TMP is limited to unallowed items to which the request relates and items with respect to which the Secretary asserts an offset to requested adjustments. The court's decision has the same effect as, and is reviewable in the same manner as, a court decision reviewing a FPAA.

Suits by individual partners

With respect to other RAAs filed by partners, if the Secretary notifies a partner that the items to which a timely request relates are to be treated as nonpartnership items, the request will be considered as a claim for refund and the partner may bring an action under section 7422 within 2 years after mailing of such notice.

Otherwise, if any part of the RAA is not allowed, the partner may, after 6 months and before 2 years from the date the request was filed, commence a suit for refund under section 7422 and the disallowed items to which the request related will be treated as nonpartnership items.

The 2-year period for filing suit may be extended by agreement between the partner and the Secretary.

An action based on unallowed items in an RAA may not be commenced after the Secretary mails notice of the commencement of a partnership proceeding to the partnership. If the 2-year period for filing suit has not expired when such notice is mailed, the rules applicable to a suit by the TMP are also applicable to other partners in the event there is no timely FPAA.

e. Statute of limitations on assessments

General rules

The period for assessment with respect to partnership items (or affected items) for any partnership taxable year shall not expire before 3 years from the date of filing the partnership return or, if later, the last date prescribed for filing such return determined without extensions. The period may be extended by agreement with any partner or, for all partners, by agreement with the TMP (or other person authorized in writing by the partnership). The agreement must be entered into before the expiration of the period to be extended. An agreement under section 6501(c)(4) (relating to agreements to extend the period for assessment) will apply to partnership items only if it expressly so provides.

Assessments may be made at any time against partners signing or actively participating in a fraudulent return. Against other partners affected by such return, the period for assessment is extended from 3 to 6 years.

The period of assessment is 6 rather than 3 years in any case where there is an omission from gross income of an amount properly includible which exceeds 25 percent of the amount of the gross income stated in the return.

Assessments may be made at any time where no partnership return is filed. For this purpose, a return filed by the Secretary on behalf of the partnership under section 6020(b) shall not be treated as a return filed by the partnership.

Suspension of limitations

The period for assessment is suspended upon mailing of a notice of FPAA until the expiration of the period during which a petition for judicial review may be filed by any partner (or, if an action is brought during such period, until the decision of the court has become final) and for one year thereafter.

Unidentified partners, inconsistency

Where a partner was not properly identified on the partnership return and a timely notice of FPAA was mailed to the TMP, or a partner's treatment of partnership items on his return did not comply with the consistency requirement in section 6222 and the inconsistency was not identified as required by that section, the assessment period will not expire until one year after the name, address, and taxpayer identification number of such partner are furnished to the Secretary.

Items becoming nonpartnership items

Where, before the expiration of the period for assessment, an item becomes a nonpartnership item by reason of an event described in section 6231(b), the period of assessment of any tax attributable to such item (or an affected item) shall not expire until one year after the date on which the item becomes a nonpartnership item.

f. Computational adjustments

Computational adjustments, generally

The procedure applicable to assessment of a deficiency will not apply to computational adjustments. Computational adjustments are changes in tax liability of a partner properly reflecting the treatment, under the rules adopted in the bill, of partnership items. The term includes all adjustments necessary to apply the results of a partnership proceeding to an indirect partner.

Adjustments necessary to correct mathematical or clerical errors (as defined in sec. 6213(g)(2)) appearing on the partnership return may be made without a partnership proceeding and opportunity for judicial review, except as to any partner who requests that such correction not be made within 60 days after notice of the correction is mailed to such partner.

Claim by partner

A claim may be filed on the ground that there was an erroneous computation of the adjustment necessary (i) to make the partnership items on the partner's return consistent with the treatment of such items on the partnership return, or (ii) to apply to the partner a settlement, a FPAA, or a final court decision relating to the treatment of partnership items. A claim may also be based on a failure to allow a refund or credit in the proper amount. A claim based on an alleged erroneous computation must be filed within 6 months after the date of mailing the notice of computational adjustment to the partner. A claim based on a failure to allow a credit or make a refund in the proper amount must be filed within 2 years after, as appropriate, (i) the date the settlement was entered into, (ii) the date on which the period for bringing an action to review a FPAA expires, or (iii) the date a court decision becomes final.

Right to file suit

To the extent a claim based on failure to properly apply computational adjustments to the partner is not allowed, suit may be filed within the period prescribed in section 6532(a). In any claim or suit involving the application of computational adjustments to the partner, the treatment of partnership items on the partnership return, under the settlement, under the FPAA, or under the court decision (as appropriate) shall be conclusive.

g. Limitations applicable to credits and refunds

Generally, the period of limitations prescribed for assessment with respect to partnership items will also apply to allowance of any credit or refund with respect to partnership items.

Credit or refund based on a timely filed RAA may be made at any time before the expiration of the period for filing suit with respect to such request.

Credit or refund based on a claim with respect to the application to the partner of a computational adjustment may be made before the expiration of the period specified in section 6532 for bringing suit on such claim.

The limitation on the period for making a credit or refund to a partner will not apply if a timely suit is brought by the partner based on an RAA or an unallowed claim with respect to a computational adjustment.

Credits or refunds attributable to partnership items, to the extent practicable, will be made without requiring that the partner file a claim.

The limitations generally applicable to the allowance of credits or refunds (subchapter B of Chapter 66) will not apply to credits or refunds of overpayments attributable to partnership items.

h. Certain other rules

When a notice of the commencement of a partnership proceeding is mailed to the TMP with respect to a partnership taxable year, the TMP is to furnish to the Secretary the names, addresses, and taxpayer identification numbers of each person who was a partner at any time during such taxable year. Revised or additional information is to be furnished at a later date by the TMP when the TMP discovers the information furnished was inaccurate or incomplete. Failure by the TMP, a pass-through partner, the representative of a 5-percent notice group, or other representative of a partner to provide any notice or take any action required under the rules or under regulations on behalf of any partner will not affect the applicability of any partnership proceeding or adjustment under the rules to such partner.

The principles of section 7481(a) shall govern in determining the date on which a court decision becomes final.

The authority granted to the Secretary by section 7602 (relating to the examination of books and witnesses) is not limited by the rules adopted by the conference agreement.

All statements, elections, requests, and furnishing of information are to be made or filed in such manner, and at such time and place, as prescribed by regulations.

The principal place of business of a partnership, if outside the United States, shall be treated as located in the District of Columbia for purposes of filing a petition in the appropriate district court under section 6226 or section 6228

The statute grants explicit authority to adopt regulations as necessary to carry out the purpose of the statutory rules.

Judicial actions brought under the rules are to be conducted in accordance with such rules of practice and procedure as the court may prescribe.

i. Small partnerships

Generally, partnerships covered by the rules include any partnership required to file a return under section 6031(a).

However, the rules do not apply to partnerships consisting of 10 or fewer partners each of whom is a natural person (other than a nonresident alien) or an estate, provided that each partner's share of any partnership item is the same as his distributive share of every other partnership item. A husband and wife (and their estates) shall be treated as one partner for purposes of this exception.

A partnership eligible to be excluded under this provision may elect to be covered by the rules. The election is binding for the year for which it is made and subsequent years unless revoked with the Secretary's consent.

j. Certain definitional and other rules

Certain definitions

The term partner, for purposes of the rules, is a direct partner in the partnership and any other person whose income tax liability is determined in whole or in part by taking into account directly or indirectly partnership items of the partnership.

The term 'partnership item' means any item required to be taken into account for the partnership's taxable year to the extent regulations provide that such item is more appropriately determined at the partnership level than the partner level. The term 'affected item' means any item to the extent it is affected by a partnership item.

A 'pass-through partner' means a partnership, estate, trust, subchapter S corporation, nominee, or other similar person through whom other persons hold an interest in a partnership with respect to which there is a partnership proceeding. The term 'indirect partner' is any person holding an interest through one or more pass-through partners.

Except as regulations may provide otherwise, a husband and wife with a joint interest in a partnership shall be treated as one person, e.g., for determining whether a partnership has more than 100 partners.

Nonpartnership items

Partnership items will become nonpartnership items as of the date that (i) the Secretary mails a notice to the partner that such items will be treated as nonpartnership items, (ii) the partner files suit under section 6228(b) after failure to allow an RAA with respect to such items, (iii) the Secretary enters into a settlement agreement with the partner with respect to such items, (iv) the items become nonpartnership items under section 6223(e) (relating to failure by the Secretary to provide timely notice to the partner of a partnership proceeding) or (v) under the Secretary's regulatory authority to treat items as nonpartnership items, such items become nonpartnership items.

The Secretary may notify a partner that a partnership item will be treated as a nonpartnership item where either (i) the partner has treated the item inconsistently with its treatment on the partnership return and properly identified the inconsistency under section 6222(b)(1)(B) (and has not subsequently field an RAA which would eliminate the inconsistency) or (ii) the partner has filed an RAA and requested adjustments would make the partner's treatment of adjusted items inconsistent with their treatment on the partnership return. Any such notification based on inconsistency on the partner's return must be mailed before the Secretary mails a notice to the TMP of the commencement of a partnership proceeding with respect to the inconsistently treated items.

Special enforcement provisions

The bill provides regulatory authority to treat items as nonpartnership items to the extent the Secretary determines their treatment as partnership items will interfere with the effective and efficient enforcement of the Internal Revenue laws. This authority extends to (i) termination assessments under section 6851 and jeopardy assessments under section 6861, (ii) criminal investigations, (iii) indirect methods of proof of income (iv) foreign partnerships, and (v) other areas to the extent determined by regulations to present special enforcement considerations.

Authority is granted to prescribe special rules by regulation determined by the Secretary to be necessary to achieve the purpose of the bill for the tax treatment of partnership items, in these cases presenting special enforcement considerations.

Determination of profits interest

The profits interst of any partner shall be determined as of the close of the partnership taxable year, except that it shall be determined immediately before the liquidation, sale, or exchange of the entire interest of a person who is not a partner at the end of such year. This determination is significant in determining whether a partner's interest is one percent or more (in partnerships with over 100 partners) and in determining whether a notice group qualifies under the 5-percent requirement applicable to such groups. This determination shall be made pursuant to regulations in the case of indirect partners.

Appeal bond to stay assessment

Section 7485, relating to bond to stay assessment and collection on the appeal of a Tax Court decision, is amended to provide for such a bond on filing a notice of appeal of a decision under section 6226 or section 6228(a). The amount of such bond fixed by the Tax Court, in the absence of a stipulation by the parties, will be based on the Tax Court's estimate of the aggregate amount of deficiencies involved.

k. Nonpartnership litigation

Other tax litigation not a bar to adjustment

A judicial determination of a partner's income tax liability not resulting from a partnership proceeding will not bar any adjustment to such liability attributable to the treatment of partnership items pursuant to a proceeding under these rules. Further, such a determination will not bar an adjustment resulting from a proceeding with respect to items that become nonpartnership items under the rules if, when they become nonpartnership items, it is no longer appropriate to include them in a separate proceeding involving other nonpartnership items. A judicial determination in a suit filed under section 6228(a) with respect to items not allowed in an RAA filed by the TMP will not bar adjustments with respect to other partnership items.

Continuation of existing rules for nonpartnership items

Existing rules relating to administrative and judicial proceedings, statutes of limitations, settlements, etc., will continue to govern the determination of a partner's tax liability attributable to nonpartnership income, loss, deductions, and credits. Neither the Secretary nor the taxpayer will be permitted to raise nonpartnership items in the course of a partnership proceeding nor may partnership items, except to the extent they become nonpartnership items under the rules, be raised in proceedings relating to nonpartnership items of a partner.

The separate statute of limitations applicable to nonpartnership items of a partner may have expired when the computational adjustment of a partner's tax liability attributable to a FPAA or final court decision is made. In such case neither the Secretary (to reduce a refund) nor a partner (to reduce an assessment) may raise nonpartnership items in determining the partner's tax liability resulting from such computational adjustment. However, if the partner has in fact overpaid his income tax liability for the taxable year with respect to which the computational adjustment was made, he may obtain credit or refund of such overpayment by filing a claim within 2 years following such overpayment, as prescribed by sections 6511 (a) and (b)(2)(B). If such claim is not allowed, suit may be filed pursuant to section 7422(a). Any overpayment which may be refunded pursuant to such a claim or suit for refund would be attributable only to nonpartnership items.

l. Foreign-based partnerships

The bill explicitly applies the partnership return filing requirement under section 6031 to any partnership which has U.S. partners (direct or indirect). Where the TMP resides outside the United States or the partnership books and records are kept outside the United States, failure to comply with the partnership return requirement or provide the return information upon request will result in disallowance of partnership losses and credits to the partners. The Secretary may by regulation waive the reporting requirement in appropriate cases. The bill also requires a return by a U.S. person who acquires or disposes of an interest in a foreign partnership except to the extent regulations provide otherwise. This requirement extends to substantial changes in the proportionate interest of a U.S. person in a foreign partnership. The return is to be in such form and provide such information as regulations require and must be filed within 90 days after the date the U.S. person becomes liable to file such return unless the Secretary, by regulation, prescribes a later date.

The tax treatment for partnership items under subchapter C of chapter 63, as added by the bill, the partnership return filing requirement under section 6031, and the return requirement relating to changes in interest in a foreign partnership are all expressly inapplicable, under the bill, to the International Telecommunications Satellite Organization and the International Maritime Satellite Organization, and any organization which is a successor to either of such organizations. Both such organizations are public international organizations established by international agreements to which the United States is a party.

m. Partnership must provide information to partners

Section 6031 is amended by the bill to require expressly that every partnership required to file a return shall furnish to every person who was a partner at any time during the partnership's taxable year a copy of such information shown on the return as may be required by regulation. The fact that the bill expressly imposes this requirement is not intended to imply that the Internal Revenue Service is without authority to impose a similar requirement under present law.

n. Effective date

The amendments relating to acquisitions, dispositions, and substantial changes in the interest of a U.S. person in foreign partnerships apply in the case of such changes after the date of enactment. All other amendments apply to partnership taxable years beginning after the date of enactment. However, pursuant to regulations, a partnership with the consent of all partners may elect to have such amendments apply to the first partnership taxable year ending after the date of enactment if the Secretary also consents.

o. Windfall profit tax audits

Under the conference agreement, windfall profit tax items are included as partnership audit items under regulations to be issued by the Treasury. Thus, the tax treatment of any partnership windfall profit tax item will be determined at the partnership level rather than the partner level. A partnership windfall profit tax item is any item relating to the computation of the windfall profit tax on crude oil produced by the partnership which the Treasury determines by regulation to be more appropriately determined at the partnership rather than the partner level. Examples of such items are (1) the removal price of crude oil, (2) the adjusted base price of the crude oil, (3) the category of the crude oil, (4) the appropriate severance tax adjustments, and (5) the net income limitation. Under regulations, the partnership will be authorized to act on behalf of its partners for purposes of the determination, examination, and collection of windfall profit tax. Thus, the partnership can be made responsible for certifying necessary withholding tax information to first purchasers and for filing quarterly and annual returns with respect to the partnership's production of domestic crude oil. When necessary, the partnership will be able to rely on certifications by its partners of their status under the windfall profit tax. On the election of one or more partners owning an interest in at least 5 percent of partnership income, this authorization will cease to apply for the entire partnership.

Under the conference agreement, each partner will remain primarily liable for the windfall profit tax on his allocable share of taxable crude oil produced by the partnership. The partner's liability will be abated to the extent of any payment of windfall profit tax by the partnership. In determining the liability of any partner for windfall profit tax purposes, each partner would be required to treat any partnership windfall profit tax item in a manner consistent with the treatment of that item on the partnership return unless the partner notifies the Secretary of an inconsistent position. Each partner will be required to certify to the partnership that partner's correct treatment under the exemption of independent stripper wells, the special rates on independent producers, the royalty owners exemption and other producer-related provisions. The partnership will compute and pay the windfall profit tax on the assumption that the certifications given by the partners are correct.

The examination and collection of tax relating to independent producer or exempt status, etc., will be conducted at the partner level. All other items are determined at the partnership level. Thus, a partner's treatment of partnership windfall profit tax items will, under regulations, be determined by reference to the treatment of such items in the hands of the partnership. Thus, for example, a partner can sue for a refund on the basis of that partner's claim of the independent producer lower rates, but can not seek a refund on the theory that oil classified as tier 2 oil by the partnership should have instead been classified as tier 3 oil.

Present law provides the Secretary with broad authority to require the keeping of records, the making of returns, and the furnishing of information relating to the windfall profit tax. It is anticipated that the Secretary will use this authority to reduce the amount of information which must be delivered to partners by the partnership in the normal course of business and to provide for a consolidated partnership return reflecting the taxes of the individual partners. In addition, the Secretary should require under this authority that partners be given access to any and all windfall profit tax information necessary for the verification of the tax computed by the partnership or to the determination of their entitlement to independent producer lower rates or royalty owner exemptions.

The bill would apply to determination, examination, and collection of windfall profit tax with respect to oil removed in taxable periods beginning after December 31, 1982, unless the partnership, each partner, each indirect partner and the Secretary consent to earlier application of the provisions.

4. Taxpayer safeguard provisions

Present law

Property exempt from levy

Present law exempts certain property from levy. Among other items, this exemption covers (1) fuel, provisions, furniture, and personal effects; (2) books and tools of a trade, business or profession; and (3) wages, salary, or other income.

For a taxpayer who is the head of a family, there is a $500 exemption for fuel, provisons, furniture, and personal effects in his household, and for arms for personal use, livestock, and poultry.

Books and tools necessary for the trade, business, or profession of the taxpayer are exempt from levy to the extent that they do not exceed $250 in aggregate value.

The exemption for wages, salary, and other income is $50 per week plus $15 per week with respect to each individual over half of whose support is received from the taxpayer, who is the spouse of the taxpayer, who is a dependent of the taxpayer, and who is not a minor child of the taxpayer with respect to whom amounts are exempt from levy pursuant to a support judgment entered prior to the date of levy.

Release of lien

Under present law, a lien may be released if the tax liability has been fully satisfied or has become legally unenforceable; or upon acceptance of a bond that is conditioned upon the payment of the amount assessed, together with all interest. There is no statutory time limit for the release of a lien.

Notice before levy

Levy upon property may be made if the taxpayer neglects or refuses to pay tax within 10 days after notice and demand. In the case of a levy upon property, other than salary or wages, there is no statutory provision that requires additional notice before levy.

Levy may be made upon the salary or wages of a taxpayer only after the Secretary has notified the taxpayer in writing of his intention to make such levy, unless there has been a finding that the collection of tax is in jeopardy. This notice must be given in person, left at the taxpayer's dwelling or usual place of business, or sent by mail to the taxpayer's last known address, no less than 10 days before the day of levy.

A levy on salary or wages is continuous from the date it is made until the taxpayer's liability is satisfied or becomes unenforceable due to lapse of time. Once the tax liability is satisfied or becomes unenforceable, the Secretary is required to promptly release the levy and notify the taxpayer of such action.

Redemption of property

The owners of real property that is sold after a seizure, their heirs, executors, or administrators, or any person having an interest therein, or a lien thereon, or any person in their behalf, may redeem the property at any time within 120 days after the sale.

Amount of damages in case of wrongful levy

In the case of an alleged wrongful levy, a person (other than the person against whom is assessed the tax out of which such levy arose) who claims an interest in, or lien on, the property levied upon may bring a civil action against the United States in a U.S. district court. If the court determines there was a wrongful levy, then the court may (1) order the return of the property if the United States is in possession thereof; (2) grant a judgment for the amount of money levied upon; or (3) grant a judgment for an amount not exceeding the amount received by the United States from the sale of property.

House bill

No provision.

Senate amendment

No provision.

Conference agreement

a. Property exempt from levy

The conference agreement increases the exemption from levy for (1) fuel, provisions, furniture, and personal effects, etc.; (2) books and tools of a trade, business, or profession; and (3) wages, salary, or other income.

The exemption for fuel, provisions, furniture, and personal effects, etc., is increased from $500 to $1,500.

The exemption for books and tools of a trade, business, or profession is increased from $250 to $1,000.

The exemption for wages, salary, and other income is increased to $75 per week plus $25 per week for the taxpayer's spouse and each dependent.

This provision applies to levies made after December 31, 1982.

b. Release of lien

The conference agreement requires a lien to be released no later than 30 days after the day on which: (1) the tax liability has been fully satisfied or has become legally unenforceable, or (2) a bond has been accepted.

This provision is effective with respect to liens (1) which are filed after December 31, 1982, (2) which are satisfied after December 31, 1982, or (3) with respect to which the taxpayer after December 31, 1982, requests the Secretary to issue a certificate of release on the grounds that the liability was satisfied or legally unenforceable.

c. Notice before levy

The conference agreement provides that levy may by made upon the salary, wages, or other property of any person with respect to any unpaid tax only after the Secretary has notified the person in writing of his intention to make such levy. This notice must be given in person, left at the dwelling or usual place of business of such person, or sent by certified or registered mail to such person's last known address, no less than 10 days before the day of levy. As under present law, a single notice wil be sufficient to cover all property of the taxpayer subject to levy.

As under present law, the notice requirement will not apply to a levy if the Secretary has made a finding that the collection of tax is in jeopardy. Moreover, the conference agreement makes no change with respect to the continuous nature of a levy upon salary or wages, or the requirements with respect to release of the levy and notice of release.

This provision applies to levies made after December 31, 1982.

d. Redemption of property

The conference agreement extends the period of time during which property that has been sold after a seizure may be redeemed from 120 days to 180 days.

This provision applies to property sold after the date of enactment.

e. Amount of damages in case of wrongful levy

The conference agreement provides that if there has been a wrongful levy and sale of property (belonging to a person other than the person against whom the tax was assessed), then the court may grant a judgment for an amount not exceeding the greater of (1) the amount received by the United States from the sale of such property, or (2) the fair market value of the property immediately before the levy.

This provision applies to levies made after December 31, 1982.

f. Notice of procedural safeguards

The conferees are concerned that in certain cases taxpayers may not be aware of the existing statutory or administrative rights and procedural safeguards that are available to them. The conferees believe that distribution of information concerning taxpayer rights at the time of the I.R.S. initial contact with the taxpayer regarding an audit and at appropriate stages during examination and collection proceedings will assure that more taxpayers are adequately apprised of their rights and the procedures available to them. Thus, the conferees request that the Internal Revenue Service consider the sufficiency and timeliness of information sent to taxpayers regarding their rights during examination, appeals, and collection. The results of this study are to be reported to the House Committee on Ways and Means and the Senate Committee on Finance.

D. Pension Provisions

1. Overall limits on contributions, benefits, and exclusions

Present law

Present law limits 1982 contributions on behalf of an employee to a qualified profit-sharing or other defined contribution plan to the lesser of 25 percent of compensation or $45,475. Annual benefits payable under a qualified defined benefit pension plan are limited to the lesser of 100 percent of compensation or $136,425 for life, beginning at age 55. The limits (set at $25,000 and $75,000 in 1974) are automatically adjusted for cost-of-living increases.

If an employee participates in a defined contribution plan and a defined benefit plan maintained by the same employer, the fraction of the separate limits used by each plan is computed and the sum of the fractions is subject to an overall limit of 1.4 (i.e., 140 percent of the otherwise applicable separate limits).

House bill

No provision.

Senate amendment

The Senate amendment makes several changes to the overall limits on contributions and benefits for an employee under a tax-qualified pension, etc., plan. The amendment (1) reduces the dollar limit for annual additions to profit-sharing plans and other defined contribution plans from $45,475 to $30,000; (2) reduces the dollar limit for annual benefits under defined benefit pension plans from $136,425 to $90,000, and requires that an interest rate assumption of at least 5 percent be used to determine whether alternative benefit forms (e.g., lump sum distributions) are within the annual benefit limit; (3) suspends cost-of-living adjustments to the dollar limits until 1986, at which time the limits will be adjusted for post-1984 cost-of-living increases (as measured by the social security benefit index), and provides that employers cannot deduct contributions to fund anticipated cost-of-living increases, (4) requires that the dollar limit ($90,000 for 1983) be actuarially reduced (using an interest rate assumption of at least 5 percent) if benefits commence before age 62 (increased from age 55); and (5) reduces the aggregate limit for an individual who participates in a defined contribution plan and a defined benefit plan of the same employer from 1.4 (140 percent of the otherwise applicable separate dollar or percentage limit) to the lesser of 1.25, as applied only to the dollar limits, or 1.4, as applied under present law.

In general, these provisions will apply to plan years beginning after December 31, 1982, except that plan amendments are required with respect to plan years beginning after December 31, 1983.

Conference agreement

The conference agreement generally follows the Senate amendment except that the dollar limit for benefits under a defined benefit plan commencing before age 62 is to be actuarially reduced (using an interest rate of not less than the greater of 5 percent or the rate specified in the plan)[1] to the equivalent of the dollar limit for benefits commencing at age 62 (age 55 where the $75,000 minimum applies). Thus, the dollar limit is not less than $75,000 at age 55 or later. For ages below 55 the limit is not less than the actual equivalent of a $75,000 annual benefit commencing at age 55. Also, for benefits commencing after age 65 the dollar limit is increased (using an interest rate not exceeding the lesser of 5 percent or the rate specified in the plan) to the equivalent of the benefit limit as applied to benefits commencing at age 65. In no event, however, could future cost-of-living increases in the dollar limit be assumed in determining actuarial equivalence.

The conference agreement revises the transition rule relating to cases where the sum of the defined benefit plan and defined contribution plan fractions exceeds 1.25 (as applied to the dollar limits). Under the provision, the Secretary of the Treasury is to prescribe regulations under which the defined contribution plan fraction (as determined for the last year ending before January 1, 1983) is reduced, so that the sum of the fractions does not exceed the aggregate limit under the conference agreement.

The conference agreement clarifies present law by providing that the employer's deduction limit for the year under a defined benefit plan may not be based on benefits in excess of the dollar limit applicable for the year (without regard to anticipated cost-of-living increases). Deductions may be based on benefits which take into account anticipated salary increases, subject to limitation described in the preceding sentence.

The conference agreement also places a $100,000 aggregate limit on the estate tax exclusion for certain retirement benefits under qualified pension, etc., plan, tax-sheltered annuities, individual retirement accounts (IRA's) and certain military retirement plans. The limit applies with respect to decedents dying after December 31, 1982.

2. Loans from retirement plans

Present law

A qualified pension, etc., plan or a tax-sheltered annuity program generally is permitted to make reasonable loans to participants other than owner-employees under an H.R. 10 plan or shareholder-employees under a subchapter S corporation plan. If a self-employed individual borrows from an H.R. 10 plan or if an individual borrows from an IRA, the loan is treated as a distribution, subject to the usual income tax rules.

House bill

No provision.

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[1] Rev. Rul. 79-90 1979-1CB 156, requires that a plan specify the actuarial assumptions used by the plan to determine benefit equivalence.

Senate amendment

The Senate amendment generally provides that a loan received by a participant under a qualified plan or a tax-sheltered annuity program is treated as a distribution to the extent that the participant's outstanding loan balance under all plans in which the participant participates exceeds $10,000. A higher limit (not to exceed $50,000) is permitted if the loan proceeds are applied towards the purchase, reconstruction, etc., of a personal residence. Loan amounts treated as distributions generally are subject to the usual income tax and withholding rules for plan distributions.

The amendment applies to loans made after July 1, 1982. Loans made before that date are not affected except to the extent that the loan is renegotiated, revised, or extended. A loan is treated as received if the proceeds are paid to or on behalf of a participant or beneficiary or if the loan is extended, etc. The amendment changes the tax treatment of loans but does not change the rules of the Employee Retirement Income Security Act of 1974 limiting the availability of loans.

Conference agreement

In general

The conference agreement follows the Senate amendment except that a loan from a tax-qualified plan, or, government plan, or tax sheltered annuity which is to be repaid within 5 years is treated as a distribution only to the extent that the amount of the loan, when added to the outstanding loan balance with respect to the employee under all plans of the employer, exceeds the lesser of (1) $50,000, or (2) one-half of the present value of the employee's nonforfeitable accrued benefit under such plans, but not less than $10,000. For this purpose, plans of separate employers which generally are treated as a single employer under the pension, etc., plan rules (sec. 414) are treated as plans of a single employer.

A loan made with respect to an employee under a qualified plan, etc., which is not required to be repaid within 5 years, is treated as a distribution. For this purpose, the period within which a loan is required to be repaid is determined at the time the loan is made. If a repayment period of less than 5 years is subsequently extended beyond 5 years, it is intended that the balance payable under the loan at the time of the extension is to be treated as distributed at the time of the extension. In addition, if payments under a loan with a repayment period of less than 5 years are not in fact made, so that an amount remains payable at the end of 5 years, the amount remaining payable is treated as if distributed at the end of the 5-year period. A loan which is treated as a distribution on account of a repayment period of more than 5 years will not be treated as other than a distribution merely because it is repaid within 5 years (whether by reason of a renegotiation of the payment period or otherwise). Of course, a loan to a beneficiary which is treated as a distribution is included in the income of the participant, if the participant is alive at the time the loan is treated as a distribution.

The conference agreement provides an exception to the 5-year repayment rule to the extent that a loan made with respect to a plan participant is applied toward acquiring, constructing, or substantially rehabilitating any house, apartment, condominium, or mobile home (not used on a transient basis) which is used or is to be used within a reasonable time as the principal residence of the participant or a member of the participant's family. The determination as to whether a dwelling is to be used as a principal residence of the participant or dependent is to be determined at the time the loan is entered into.

Certain mortgage loans

Under the conference agreement, investments (including investments in residential mortgages) which are made in the ordinary course of an investment program will not be considered as loans, if the amount of the mortgage loan does not exceed the fair market value of the property purchased with the loan proceeds. An investment program exists, for example, when trustees determine that a specific percentage or amount of plan assets will be invested in residential mortgages under specified conditions. However, mortgage loans made as a result of the direction of investments of an individual account will not be considered as made under an investment program and no loan which benefits an officer, director, or owner or his beneficiaries will be treated as an investment. In addition, the agreement makes no changes to the present-law prohibited transaction rules and fiduciary standards for qualified pension, etc., plans and does not restrict the rules of present law under which certain loans are treated as distributions.

Effective dates

The conference agreement applies to loans made after August 13, 1982.

Amounts outstanding on August 13, 1982, under a loan which is renegotiated, extended, revised, or renewed after such date will not be treated as made on the date of the renegotiation, etc., to the extent such amounts are required to be, and are repaid on or before August 13, 1983. Thus, such amounts will continue to be treated as amounts outstanding with respect to the participant on August 13, 1982.

The conferees intend that a scheduled change in the interest rate charged on a loan balance (e.g., a variable rate contract) will not be treated as a revision or renegotiation of the loan.

3. Parity under the qualified plan rules for corporate and noncorporate employers; group-term life insurance

Present law

Under present law, plans which benefit self-employed individuals, owner-employees, or shareholder-employees of subchapter S corporations are subject to additional, more restrictive, qualification requirements designed to limit benefits for such individuals and provide additional protections for rank-and-file employees.

House bill

No provision.

Senate amendment

The Senate amendment increases the dollar limits applicable to defined contribution H.R. 10 plans, plans of subchapter S corporations, and SEPs, from $15,000 in 1982 to $20,000 in 1983, $25,000 in 1984, and $30,000 in 1985. The 15-percent of earned income limit is not changed. To provide a similar increase in the level of benefits permitted under a defined benefit H.R. 10 plan or subchapter S corporation plan, the compensation taken into account in determining permitted annual benefit accruals is increased from $100,000 to $133,000 in 1983, $167,000 in 1984 and $200,000 in 1985.

Beginning in 1986, the bill adjusts the limits for post-1984 cost-of-living increases.

Conference agreement

In general

The conference agreement generally eliminates distinctions in the tax law between qualified pension, etc., plans of corporations and those of self-employed individuals (H.R. 10 plans). The agreement (1) repeals certain of the special rules, for H.R. 10 plans, (2) extends other of the special rules to all qualified plans, including those maintained by corporate employers, and (3) generally applies the remainder of the special rules, with appropriate modifications, only to those plans (whether maintained by a corporate or noncorporate employer) which primarily benefit the employer's key employees (top-heavy plans). The top-heavy plan rules are provided in addition to the usual rules for plan qualification.

The special rules for H.R. 10 plans which are repealed include those which (1) set lower limits on contributions and benefits for self-employed individuals, (2) prevent certain H.R. 10 plans from limiting coverage to a fair cross section of employees, and (3) prohibit integration with social security.

The special rules for H.R. 10 plans which are extended to all qualified plans are certain of those rules relating to (1) distributions made to the employee or to the employee's beneficiaries after the employee's death, and (2) integration of a defined contribution plan with social security.

The special rules for H.R. 10 plans which generally are extended (with modifications) to plans of corporate and noncorporate employers which primarily benefit key employees (top-heavy plans) include those rules relating to (1) includible compensation, (2) vesting (alternative schedules are provided) and (3) distributions. The rules for a top-heavy plan also require that such a plan provide a non-key employee a nonintegrated minimum benefit or a nonintegrated minimum contribution, and in some cases reduce the aggregate limit on contributions and benefits for a key employee who is covered by more than one plan of an employer.

These provisions apply for years beginning after December 31, 1983.

Repeal of rules for H.R. 10 plans

Deductible contributions and permitted benefit accruals

The conference agreement generally repeals the special deduction limits (sec. 404(e) (1), (2), and (4)) for contributions on behalf of a self-employed individual under an H.R. 10 plan. Conforming amendments are made with respect to simplified employee pensions and plans of subchapter S corporations.

In addition, the conference agreement repeals the special qualification rules for a defined benefit plan which covers a self-employed individual or a shareholder-employee of a subchapter S corporation (sec. 401(j)). Thus, defined benefit plans which cover a self-employed individual or a shareholder-employee of a subchapter S corporation will be subject to the rules applicable to other defined benefit plans.

Earned income

For purposes of the pension rules, the conference agreement revises the definition of earned income of a self-employed individual so that the amount of earned income corresponds to the amount of compensation of a common-law employee. Under the agreement, earned income is computed after taking into account amounts contributed by the employer to a qualified plan to the extent a deduction is allowed for the contributions. Also, in this regard, no change is made to the present-law rule (sec. 401(d)(11)) for owner-employees which has the effect of limiting the earned income which may be taken into account under the pension rules to that derived from the trade or business with respect to which the plan is established.

In addition, no change is made to the present-law rules under which no deduction is allowed for contributions to an H.R. 10 plan on behalf of a self-employed individual to the extent that the contributions are allocable to the purchase of incidental life, health, or accident insurance (sec. 404(e)(3)), and under which a self-employed individual generally is denied a basis in amounts applied under an H.R. 10 plan to purchase life insurance protection for the individual (sec. 72(m)(2)).

Coverage

The agreement repeals the additional qualification requirement under which an H.R. 10 plan benefiting an owner-employee generally is required to benefit all employees who have completed at least three years of service with the employer (sec. 401(d)(3)(A)).

The agreement retains the special rules for H.R. 10 plans under which all employees of all unincorporated trades or businesses controlled by an owner-employee (or owner-employees) are treated as if employed by a single trade or business for purposes of the nondiscrimination rules (sec. 401(a)(9) and (10)).

Employee contributions

The agreement repeals the special rules precluding employer contributions on behalf of an owner-employee under an H.R. 10 plan in excess of the deduction limit (sec. 401(d)(5)), and those rules limiting or precluding mandatory or voluntary employee contributions by an owner-employee (sec. 4972). The agreement also repeals the six-percent excise tax on excess contributions made on behalf of an owner-employee.

Miscellaneous restrictions

The following special H.R. 10 plan rules are also repealed:

(1) the requirement that a profit-sharing plan provide a definite contribution formula for employees who are not owner-employees (sec. 401(d)(2)(B));

(2) the requirement that an owner-employee must consent to participate (sec. 401(d)(4)(A));

(3) the requirement that the plan trustee be a bank or other approved financial institution (sec. 401(d)(1));

(4) the prohibition against contributions on behalf of an owner-employee for the five taxable years following an early withdrawal by the owner-employee (sec. 401(d)(5)(C)): and

(5) the denial of the $5,000 income exclusion for death benefits paid with respect to a self-employed individual under the plan (sec. 101(b)).

Nothing in the agreement requires that an H.R. 10 plan delete these provisions. For example, an employer may prefer that an H.R. 10 plan continue to provide that an owner-employee must consent to participate, thereby permitting an owner-employee to elect against plan participation.

Extension of certain H.R. 10 rules to all plans

Required distributions

The agreement extends to all qualified plans the requirement that payment of a participant's benefits must commence not later than (1) the taxable year in which the participant attains age 70½, or (2) if later, the year in which the participant retires (sec. 401(a)(9)).

In addition, if a participant dies before the entire interest is distributed, the entire remaining interest generally must be distributed to the participant's beneficiary or beneficiaries within 5 years. However, this rule does not apply if the distribution has commenced to the participant and is payable over a period which does not exceed the joint life expectancy of the participant and the participant's spouse. A conforming change is made to the IRA distribution rules.

Integration with social security

The bill extends to all qualified defined contribution plans a rule under which the tax rate applicable to employers for old age, survivors, and disability insurance (OASDI) under social security is the maximum rate at which employer contributions can be reduced under plans that are integrated with social security. This provision is designed to decrease the extent of integration in defined contribution plans without increasing the extent of integration in any plan.

For 1982, the employer's tax rate with respect to OASDI benefits under social security is 5.4 percent, and the taxable wage base is the first $32,400 of an employee's pay. Thus, if the provisions were applicable for 1982, a profit-sharing plan could provide contributions of 5.4 percent of 1982 pay in excess of $32,400 and no contributions for 1982 with respect to the first $32,400 of pay. Similarly, if a plan provided for 1982 contributions of 10 percent of pay in excess of $32,400, it would integrate only if it provided for 1982 contributions of at least 4.6 percent (10% minus 5.4%) with respect to the first $32,400 of pay. The same rules apply to a self-employed individual.

The wage base and tax rates which apply for any plan year are the wage base and tax rates in effect on the first day of the plan year.

The remaining present-law rules which restrict integration with social security under an H.R. 10 defined contribution which benefits an owner-employer are repealed.

Additional qualification requirements for top-heavy plans

In general

Under the agreement, additional qualification requirements are provided for plans which primarily benefit an employer's key employees (top-heavy plans). These additional requirements (1) limit the amount of a participant's compensation which may be taken into account, (2) provide greater portability of benefits for plan participants who are non-key employees, (3) provide minimum nonintegrated contributions or benefits for plan participants who are non-key employees, and (4) reduce the aggregate limit on contributions and benefits for certain key employees. Further, additional restrictions are placed on distributions to key employees.

Top-heavy plans

Under the agreement, a defined benefit plan is a top-heavy plan for a plan year if, as of the determination date, (1) the present value of the accumulated accrued benefits for participants who are key employees for the plan year exceeds sixty percent of the present value of the accumulated accrued benefits for all employees under the plan, or (2) the plan is part of a top-heavy group. A defined contribution plan is a top-heavy plan for a plan year if, as of the determination date, (1) the sum of the account balances of participants who are key employees for the plan year exceeds sixty percent of the sum of the account balances of all employees under the plan, or (2) the plan is a part of a top-heavy group. Under these rules, a simplified employee pension is considered a defined contribution plan, and at the election of the employer, the account balance of any employee covered by a simplified employee pension is deemed to be the sum of the employer contributions made on the employee's behalf.

The determination date for any plan year generally is the last day of the preceding plan year. However, in the case of the first plan year, the determination date is the last day of that year. Further, to the extent provided in regulations, the determination date may be determined on the basis of a year other than a plan year.

Top-heavy groups

The agreement also provides rules under which two or more plans of a single employer are aggregated to determine whether the plans, as a group, are top-heavy. The aggregation group must include (1) any plan which covers a key employee, and (2) any plan upon which a plan covering a key employee depends for qualification under the Code's coverage or antidiscrimination rules (secs. 401(a)(4) and 410). In addition, in testing for top-heaviness, an employer may elect to expand the aggregation group to take into account any other plan maintained by the employer, if such expanded aggregation group continues to satisfy the coverage and antidiscrimination rules.

An aggregation group is a top-heavy group if, as of the determination date, the sum of (1) the present values of the accumulated accrued benefits for key employees under any defined benefit plans included in the group, and (2) the sum of the account balances of key employees under any defined contribution plans included in the group, exceeds 60 percent of the same amount determined for all participants under all plans included in the group. If an aggregation group is a top-heavy group, each plan required to be included in the group is a top-heavy plan. Of course, no plan included in the aggregation group at the election of the employer is subject to the top-heavy plan rules on account of such election.

The top-heavy group rules apply to all plans of related employers which are treated as a single employer (sec. 414).

Additional rules

For purposes of determining the present value of accumulated accrued benefits under a defined benefit plan and the sum of the account balances under a defined contribution plan, benefits derived from both employer contributions and employee contributions generally are taken into account. However, accumulated deductible employee contributions) under a plan are to be disregarded. In addition, to insure relative stability and to preclude distortions under the top-heavy plan computation, the present value of the accrued benefit of a participant in a defined benefit plan or the account balance of a participant in a defined contribution plan generally includes any amount distributed with respect to the participant under the plan within the five-year period ending on the determination date.

A rollover contribution (or similar transfer) made after December 31, 1983, generally is not taken into account under the transferee plan for purposes of the top-heavy plan computation. The conferees intend that this rule will not apply if the contribution (or transfer) is made incident to a merger or consolidation of two or more plans or the division of a single plan into two or more plans. In addition, the conferees intend that this rule will not apply to rollover contributions (or transfers) between plans of the same employer, including plans of related employers which are treated as a single employer (sec. 414). Of course, in any case in which a rollover contribution (or transfer) is required to be taken into account under the transferee plan, the amount distributed by the transferor plan is not also taken into account under the transferor plan.

If an employee ceases to be treated as a key employee, the employee's accrued benefit under a defined benefit plan or the employee's account balance under a defined contribution plan is disregarded under the top-heavy plan computation for any plan year following the last plan year for which the employee was treated as a key employee.

Key employees

Key employees generally include employees who (1) are officers (but in no event will officers of any employer include more than 50 employees or, if lesser, the greater of 3 employees or 10 percent of all employees),[1] (2) are one of the 10 employees owning the largest interests in the employer (there are not 10 employees owning greater interests than the employee), (3) own more than a five-percent interest in the employer, or (4) own more than a one-percent interest in the employer and have annual compensation from the employer in excess of $150,000. An employee is considered an officer, or as owning an interest in the employer, if the employee was an officer, or owned such an interest, at any time during the plan year or the four preceding plan years. In the case of an employer which has more officers than are required to be counted as key employees, the officers to be taken into account are the officers with the highest compensation.

Under the agreement, an employee is considered as owning more than a five-percent interest in a corporate employer if the employee owns more than five percent of the employer's outstanding stock or stock possessing five percent of the total combined voting power of all stock of the employer. An employee is also treated as owning stock owned by certain members of the employee's family or, in certain cases, by partnerships, estates, trusts, or corporations in which the employee has an interest (sec. 318). The same rules apply to determine whether an individual owner is a one-percent owner.

In the case of an employer which is not a corporation, ownership will be determined in accordance with regulations prescribed by the Secretary. The conferees intend that these regulations be based on principles similar to the principles of section 318. In addition, to determine whether a self-employed individual who is a one-percent owner, is a key employee, compensation means earned income from the trade or business with respect to which the plan is maintained.

Qualification rules

These additional rules for top-heavy plans are tax-qualification requirements. Thus, a top-heavy plan is a qualified plan, and a trust forming part of a top-heavy plan is a qualified trust only if the additional requirements are met. Except as the Secretary of the Treasury may provide by regulations, a plan (whether or not top-heavy in fact) will constitute a qualified plan only if the plan includes provisions which will automatically take effect if the plan becomes a top-heavy plan and which meet the additional qualification requirements for top-heavy plans.

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[1] As under present law, the determination as to whether an employee is an officer is to be determined upon the basis of all the facts and circumstances, including, for example, the source of the employee's authority, the term for which elected or appointed, and the nature and extent of the employee's duties. As generally accepted in connection with corporations, the term "officer" means an administrative executive who is in regular and continued service. It implies continuity of service and excludes those employed for a special and single transaction, or those with only nominal administrative duties. Thus, for example, all the employees of a bank who have the title of vice president or assistant vice president would not automatically be considered to be officers. See, for example, Rev. Rul. 80-314, 1980-2 C.B. 152.

Includible compensation

For any plan year for which a plan is a top-heavy plan, only the first $200,000 of an employee's compensation may be taken into account in determining contributions or benefits under the plan. Beginning in 1986, this $200,000 limit will be adjusted under the same rules used to adjust the overall limits on contributions and benefits. For a self-employed individual, compensation means earned income as redefined by the conference agreement.

Vesting

For any plan year for which a plan is a top-heavy plan, an employee's right to the accrued benefit derived from employer contributions must become nonforfeitable (sec. 411(a)) under a vesting schedule which satisfies one of two alternative schedules provided by the agreement. These vesting schedules apply to all accrued benefits, whether or not the accrued benefits are required by the top-heavy plan rules.

A plan will satisfy the first alternative vesting schedule (three-year full vesting) if an employee who has at least three years of service with the employer or employers maintaining the plan has a nonforfeitable right to 100 percent of his accrued benefit derived from employer contributions. As under present law, a plan which provides three-year, 100 percent vesting will satisfy the participation requirements if the plan provides that an employee who is at least 25 years old, with three years of service, is eligible to participate.

A plan will satisfy the second alternative vesting schedule (six-year graded vesting) if an employee has a nonforfeitable right to at least 20 percent of the accrued benefit derived from employer contributions at the end of two years of service, 40 percent at the end of three years of service, 60 percent at the end of four years of service, 80 percent at the end of five years of service with the employer, and 100 percent at the end of six years of service with the employer.

For purposes of determining service under these vesting schedules, the present-law rules (sec. 411) relating to years of service, breaks in service, and certain permitted forfeitures etc., apply. Accordingly, all years of service with the employer generally are to be taken into account, including years of service completed prior to enactment and service during periods for which a plan is not a top-heavy plan.

Minimum nonintegrated benefit for non-key employees

In addition, a qualified pension, etc., plan which is a top-heavy plan must provide a minimum benefit or contribution for each non-key employee who is a participant in the plan.

Under the conference agreement, any individual excluded from coverage under a defined benefit or defined contribution plan because of compensation below a specified amount, or any individual considered to be a participant for purposes of the coverage requirements (sec. 410) must be provided the applicable minimum contribution or benefit.

For a plan year for which a defined benefit plan is a top-heavy plan, each plan participant who is not a key employee for the year generally must accrue a benefit which, when expressed as an annual retirement benefit, is not less than two percent of the employee's average annual compensation from the employer during the employee's testing period, multiplied by the employee's years of service with the employer. However, an employee's minimum benefit is not required to exceed 20 percent of such average annual compensation. All years of an employee's service otherwise required to be taken into account under the plan generally are required to be taken into account under the minimum benefit rules, except a year of service (1) ending before the date of enactment, or (2) within which ends a plan year for which the plan is not a top-heavy plan.

For purposes of the minimum benefit rules, only benefits derived from employer contributions (other than amounts employees have elected to defer (e.g. under a salary reduction cash or deferred arrangement)) to the plan are taken into account, and an employee's social security benefits are disregarded. Thus, the required minimum benefit for an employee may not be eliminated or reduced on account of the employee's social security benefits attributable to contributions by the employer (i.e., the minimum benefit is a "nonintegrated" benefit).

The term annual retirement benefit is defined as a benefit payable annually in the form of a life annuity (with no ancillary benefits) beginning at the normal retirement age. An employee's testing period is the period of the employee's consecutive years of service (not exceeding five) during which the employee had the greatest aggregate compensation from the employer. However, a year of service (and compensation paid to the employee during such year) need not be included in the employee's testing period if it ends before the date of enactment or begins within or after the last plan year for which the plan is a top-heavy plan.

Minimum nonintegrated contribution for non-key employees

For a plan year for which a defined contribution plan is a top-heavy plan, the employer generally must contribute on behalf of each plan participant who is not a key employee for the year an amount not less than three percent of the participant's compensation. However, if the employer's contribution rate for each participant who is a key employee for the plan year is less than three percent, the required minimum contribution rate for each non-key employee generally is limited to not more than the highest contribution rate for any key employee. For example, if, under a profit-sharing plan, no amount is contributed by the employer for any key employee, then under this limitation no contribution is required under the minimum contribution rules for any non-key employee. Under the minimum contribution rules, reallocated forfeitures are taken into account as employer contributions.

However, the limitation to the rate of contributions for key employees does not apply with respect to a defined contribution plan upon which a defined benefit plan depends for qualification under the Code's coverage or antidiscrimination rules, if the defined benefit plan benefits a key employee (or if a plan which benefits a key employee also depends upon the defined benefit plan). Under such circumstances, the required minimum contribution rate for a non-key employee is in every case three percent even if the contribution rate on behalf of a key employee is less than 3 percent. For purposes of the limitation, as well as for purposes of the minimum contribution rules generally, all defined contribution plans of the employer are considered a single plan.

To determine the contribution rate for an employee (including a key employee), the employer contributions and reallocated forfeitures on behalf of the employee for the year are divided by the employee's total compensation (or, with respect to a self-employed individual, the individual's earned income) from the employer for the year, not to exceed $200,000. Amounts paid by the employer for the year to provide social security benefits for the employer are disregarded. Thus, the required minimum contribution for a non-key employee may not be eliminated or reduced on account of benefits attributable to taxes paid by the employer under social security (i.e., the minimum contribution is a "nonintegrated" contribution). Similarly, the employer contribution rate for a key employee is determined without regard to employer contributions under social security. For example, if a plan is integrated with social security by providing key employees with employer contributions equal to 5 percent of compensation in excess of $32,400, the contribution rate for an employee whose total compensation is $50,000 is 1.76 percent ((0.05 × $17,600) ÷ $50,000).

No duplication of minimum benefits for non-key employees under a top-heavy group

If a non-key employee participates in both a defined benefit plan and a defined contribution plan maintained by an employer, the employer is not required by this section to provide the non-key employee with both the minimum benefit and the minimum contribution.

Rules are also provided to preclude inappropriate omissions or required duplication of minimum benefits or contributions. It is anticipated that these rules would preclude an employee who is covered under more than one plan from receiving lower benefits or contributions than that employee would receive if covered under one plan. Similarly, larger total benefits should not be required merely because an employee is covered under more than one plan (except as required where the limit of 1.0 is exceeded by a top-heavy plan). For example, if an employee participates in a top-heavy money purchase pension plan that provides an annual nonintegrated contribution rate of 5 percent of compensation and a defined benefit plan that provides an annual benefit of 1 percent of pay, the employer would not be required to provide an additional 1-percent benefit for non-key employees participating in the defined benefit plan.

Of course, contributions to either plan on behalf of the non-key employee may otherwise be required (for example, by reason of the nondiscrimination rules). In any case in which separate plans are required to be considered together for purposes of the coverage or nondiscrimination rules, the required minimum benefit or minimum contribution may of course be taken into account. However, two plans are not necessarily comparable merely because one plan provides the required minimum benefit while the other provides the required minimum contribution. Similarly, the fact that two plans both provide the required minimum benefit, or that two plans both provide the required minimum contribution, does not insure that the two plans, as a whole, are comparable.

Aggregate limit on contributions and benefits for key employees

The agreement includes additional rules with respect to the aggregate limit on benefits and contributions (sec. 415(e)) for a key employee who participates in both a defined benefit plan and a defined contribution plan which are included in a top-heavy group. Unless certain requirements are met, for any year for which the plans are included in the top-heavy group, the aggregate limit for the key employee is the lesser of 1.0 (as applied only to the dollar limits) or 1.4 (as determined under present law). However, the aggregate limit is increased to the lesser of 1.25 (as applied only to the dollar limits) or 1.4 (as under present law) if the plans of the employer in which the key employee participates (1) meet the requirements of the concentration test, and (2) provide either an extra minimum benefit (in the case of the defined benefit plan) or an extra minimum contribution (in the case of the defined contribution plan) for non-key employees participating in the plans. The extra contribution or benefit is in addition to the minimum contribution or benefit required for all top-heavy plans.

The concentration test is generally satisfied with respect to a key employee for a year if, as of the last determination date before the first day of such year, the sum of (1) the present value of the accumulated accrued benefits for key employees under the defined benefit plans of the employer in which the key employee participates, and (2) the sum of the account balances of key employees under the defined contribution plans of the employer in which the key employee participates is not greater than 90 percent of the same amount determined for all participants under the plans. For purposes of this computation, the rules for determining whether two or more plans constitute a top-heavy group apply.

The requirement for an extra minimum benefit for non-key employees is satisfied for a year if, for the plan year ending with or within such year, each non-key employee who is a participant in a defined benefit plan of the employer in which the key employee is a participant accrues an extra benefit which, when expressed as an annual retirement benefit, is not less than the lesser of (1) one percent of the employee's average annual compensation, multiplied by the employee's years of service with the employer, or (2) 10 percent of such average annual compensation. This extra minimum benefit generally is determined in the same manner as the minimum benefit required under the rules for a top-heavy defined benefit plan. However, for purposes of the extra minimum benefit, a year of service is required to be taken into account only if (1) such year of service includes the last day of a plan year for which the plan is a top-heavy plan (or included in a top-heavy group), and (2) such plan year ends with or within a year for which the aggregate limit of the key employee exceeds 1.0 (as applied to the dollar limits).

The requirement for an extra minimum contribution is satisfied with respect to a key employee for a year if, for the plan year ending with or within such year, the employer contributes on behalf of each non-key employee who is a participant in a defined contribution plan in which the key employee is a participant an extra amount not less than the amount equal to one percent of the employee's compensation for the year. Accordingly, the extra minimum contribution generally is determined under the rules for top-heavy defined contribution plans.

In some cases, the aggregate of a key employee's accrued benefit under an employer's defined benefit plans and annual additions under the employer's defined contribution plans may exceed 1.0 (as applied to the dollar limits) at the time the key employee becomes subject to an aggregate limit of 1.0. In such a case, the key employee is permitted no further benefit accruals under the defined benefit plans and no additional employer contributions under the defined contribution plans until (1) the aggregate of the key employee's accrued benefits and annual additions is less than 1.0 (as applied to the dollar limits), or (2) the aggregate limit for the key employee is increased to 1.25 (as applied to the dollar limits) under the bill. Of course, in no event are further benefit accruals permitted if the aggregate of the employee's accrued benefit and annual additions exceeds 1.25 (as applied to the dollar limit) or 1.4 (as applied under present law).

Distributions to key employees

The agreement also provides new rules for distributions from top-heavy plans to key employees. If a distribution is made to a key employee before he attains age 59½, an additional income tax is imposed equal to 10 percent of the amount includible in income, unless the distribution is made on account of death or disability.

In addition, a top-heavy plan must provide that distributions to a key employee will commence no later than the taxable year in which the key employee attains age 70½, whether or not he separates from service in that year. As under present law, the required distributions must be made in such a manner that more than 50 percent of the total benefits for the employee are payable to the employee over the employee's life expectancy (or the joint life expectancy of the employee and the employee's spouse).

Organizations performing management functions

The conference agreement expands the class of employers which, under the present-law rules for affiliated service groups (sec. 414(m)), are to be treated as a single employer for purposes of certain of the tax-law rules for qualified pension, etc., plans (including the rules for top-heavy plans), cafeteria or medical reimbursement plans, or simplified employer pensions (SEPs). Under the provision, if an organization's principal business is performing, on a regular and continuing basis, management functions for another organization, the person performing the functions and the organization for whom the functions are performed are treated as a single employer.

Under the provision, any person related to the organization performing the management functions is also included in the group which is treated as a single employer. An organization related to the organization for whom the functions are performed is included in the group under the management function rules, if the management functions are also performed, on a regular and continuing basis, for such related organization. However, the provision does not change present law under which aggregation of employers is otherwise required.

For purposes of the provision, the term "organization" includes an individual, corporation, partnership, etc. Whether organizations are related is determined under present law (sec. 103(b)(6)(C).

The conferees intend that the provision is to apply only where the management functions performed by one person for another are functions historically performed by employees, including partners or sole proprietors in the case of an unincorporated trades and businesses. For this purpose, the present-law rules relating to affiliated service organizations and to services historically performed by employees in the case of an affiliated service organization are to apply.

Employee leasing

The conference agreement also provides that, for purposes of certain of the tax-law rules for qualified pension, etc., plans (including the rules for top-heavy plans) and SEPs, an individual (a leased employee) who performs services for another person (the recipient) may be treated as the recipient's employee where the services are performed pursuant to an agreement between the recipient and a third person (the leasing organization) who is otherwise treated as the individual's employer. Under the provision, the individual is to be treated as the recipient's employee only if the individual has performed services for the recipient (or for the recipient and persons related to the recipient) on a substantially full-time basis for a period of at least 12 months, and the services are of a type historically performed by employees in the recipient's business field. For this purpose, the present-law rules relating to services historically performed by employees in the case of an affiliated service organization are to apply.

The employee leasing rules do not apply where services in a particular business field historically have been performed by one person for another. For example, some prepaid health care service programs organized on a group practice basis involve two or three components: the health plan, a separate medical group that provides or arranges physicians' services to the health plan members, and often a related hospital. The hospital and the medical group each may employ its own staff (nurses, technicians, etc.), but both sets of employees may be jointly managed. Alternatively, the staff that supports the medical group may be employed by the health plan. These forms of operation are well established in the group practice prepaid health care field. The conferees intend that the "historically performed" exception is to apply in these cases (whether the form of operation is currently in effect or put into effect for existing components of an established group practice prepaid health care service program or for the components of a new program) if the health plan, the hospital, and the medical group provide substantially similar, though not necessarily exactly equivilent retirement benefits through tax qualifed plans to salaried nonunion employees and partners.

For purposes of determining whether a pension, etc., plan or a SEP maintained by the recipient satisfies the applicable tax-law requirements, the leased employee is treated as the recipient's employee for periods after the close of the 12-month period described in the preceding paragraph. However, the leased employee's years of service for the recipient are determined by taking into account the entire period for which the leased employee performed services for the recipient (or for a related person).

Under the provision, contributions or benefits for the leased employee which are provided by the leasing organization under a qualified plan or a SEP maintained by the leasing organization are to be treated as if provided by the recipient to the extent such contributions or benefits are attributable to services performed by the leased employee for the recipient.

Under the provision, an individual who otherwise would be treated as a recipient's employee will not be treated as such an employee, if certain requirements are met with respect to contributions and benefits provided for the individual under a qualified money purchase pension plan maintained by the leasing organization. Such a plan qualifies if it provides that (1) an individual is a plan participant on the first day on which the individual becomes an employee of an employer maintaining the plan, (2) each employee's rights to or derived from employer contributions under the plan are nonforfeitable (sec. 411(a)) at the time the contributions are made, and (3) amounts are to be contributed by the employer on behalf of an employee at a rate not less than 7½ percent of the employee's compensation for the year (the 7½ percent contribution is not to be reduced by integration with social security).

For purposes of the provision, the term person includes individuals and organizations (corporations, partnerships, etc.). Whether persons are related persons is determined under present law (sec. 103(b)(6)(C)).

The provision authorizes the Secretary of the Treasury to prescribe regulations under which a leased employee will not be treated as the recipient's employee, notwithstanding that the provision may otherwise apply. Under the conference agreement, the Secretary is to prescribe such regulations where it is determined that to treat a leased employee as the recipient's employee is not appropriate, taking into account the purposes underlying those qualified plan rules with respect to which the provision applies.

Certain corporations performing personal services

Under the conference agreement, if a corporation, the principal activity of which is the performance of personal services substantially all of which are performed by employee-owners for or on behalf of another corporation, partnership, or entity (including related parties), is availed of for the principal purpose of evasion or avoidance of Federal income tax by securing for any employee-owner significant tax benefits which would not otherwise be available, then the Secretary may allocate all income, as well as such deductions, credits, exclusions, etc., as may be allowable, between or among the corporation and employee-owners involved. For this purpose, an employee-owner is defined as any employee who owns (after application of the attribution rules under section 318) more than 10 percent of the outstanding stock of the corporation. The conferees intend that the provisions overturn the results reached in cases like *Keller* v. *Commissioner,* 77 TC 1014 (1981), where the corporation served no meaningful business purpose other than to secure tax benefits which would not otherwise be available.

The provision applies to taxable years beginning after December 31, 1982.

Disincorporation relief

The conferees understand that a number of personal service corporations may wish to liquidate when the parity provisions of the conference agreement take effect. Therefore, a transitional rule is provided under which personal service corporations may, during 1983 or 1984, complete a one-month liquidation under section 333 of the Code without the risk that the corporation would incur tax on its unrealized receivables. Of course, the income represented by unrealized receivables will retain its character as ordinary income and will be fully recognized by the distributee shareholder upon subsequent collection or other disposition.

Group-term life insurance

The conference agreement also provides that the income exclusion for employer-provided group term life insurance (sec. 79) will apply with respect to a key employee only if the life insurance is provided under a program of the employer which does not discriminate in favor of key employees as to (1) eligibility to participate, or (2) the life insurance benefits provided under the plan.

A program of an employer providing group-term life insurance for employees generally will not be considered to discriminate in favor of key employees as to eligibility to participate if (1) the program benefits at least 70 percent of all employees, (2) at least 85 percent of all participating employees are not key employees, or (3) the program benefits employees who qualify under a classification set up by the employer and found by the Secretary of the Treasury not to discriminate in favor or key employees. Alternatively, a program of an employer providing group-term life insurance which is provided under a cafeteria plan (sec. 125) will not be considered to discriminate in favor of key employee as to eligibility to participate if the eligibility rules for cafeteria plans are satisfied. For purposes of the provision's rules relating to eligibility to participate, employees of certain related employers would generally be treated as if employed by a single employer. However, the following employees could be excluded from consideration: (1) those who have not completed 3 years of service with the employer, (2) part-time and seasonal employees, and (3) nonresident aliens who receive no U.S. source income from the employer. For this purpose, part-time employees are those whose customary employment is for not more than 20 hours in any one week, and seasonal employees are those whose customary employment is for not more than 5 months in any calendar year. In addition, employees not covered by the program but covered by a collective bargaining agreement need not be taken into account if group-term life insurance was the subject of good faith bargaining between the employer and employee representatives.

A program of an employer providing group-term life insurance for employees will not be considered to discriminate in favor of key employees as to the benefits provided, if the program does not discriminate in favor of such employees with regard to the type and amount of the benefits. For this purpose, group-term life insurance benefits will not be considered to discriminate merely because the amount of life insurance provided employees bears a uniform relationship to compensation. Of course, the requirement that group-term life insurance benefits be nondiscriminatory can be satisfied where, under the facts and circumstances, no discrimination in favor of key employees occurs. For example, the requirement would be satisfied when the life insurance benefits are a level dollar amount which is the same for all covered employees.

The conferees intend that the Secretary of the Treasury is to revise the tables for computing the amount includible in an employee's gross income on account of employer-provided group-term life insurance. The conferees further intend that the tables be periodically revised to reflect current group-term life insurance costs.

Effective dates

The agreement's provisions relating to parity between corporate and noncorporate employers, top-heavy plans, organizations performing management functions, employee leasing, and group-term life insurance apply to years beginning after December 31, 1983.

The provisions relating to certain corporations performing personal services applies to taxable years beginning after December 31, 1982.

4. Retirement savings for church employees

Present law

Under present law, public schools and certain tax-exempt organizations (including churches) may contribute to a tax-sheltered annuity contract for an employee. Annual contributions excluded from an employee's income are limited to 20 percent of the employee's compensation multiplied by the number of the employee's years of service with the employer, reduced by amounts already contributed by the employer. Employer contributions to a tax-sheltered annuity are also subject to the overall limit on annual additions to tax-favored retirement savings arrangements. Special one-time elections increase the overall limit for a year to allow contributions in that year that are permitted under the exclusion allowance on account of prior years of service. The elections are not available to most church employees.

House bill

No provision.

Senate amendment

The Senate amendment revises the present-law tax-sheltered annuity rules as they apply to church employees by (1) providing a minimum exclusion allowance equal to the lesser of $3,000 or 100 percent of compensation for employees with adjusted gross income of $17,000 or less; (2) providing that all years of service with organizations that are part of a particular church are treated as years with one employer; (3) extending to all church employees the special catchup elections to increase the annual contribution limit; (4) providing an additional election for church employees which increases the contribution limit by up to $10,000 for any year, subject to a $40,000 lifetime cap; (5) permitting churches to maintain segregated defined contribution retirement savings programs pursuant to the tax-sheltered annuity rules; and (6) providing a special retroactive correction period for church plans.

These changes apply to taxable years beginning after December 31, 1981, except that the provision permitting retroactive amendments applies after July 1, 1982.

Conference agreement

The conference agreement follows the Senate amendment with regard to permitted contributions for church employees under the exclusion allowance and annual contribution limit for tax-sheltered annuities.

The conference agreement also follows the Senate amendment by allowing a church which maintains a tax-sheltered annuity, retirement income account, or pension plan, a retroactive amendment period if the annuity, account or plan, is required to be amended by reason of any law, or any regulation, ruling or other action under the tax laws. During the correction period, the annuity, account, or plan would be treated as satisfying the applicable tax-law requirement. To qualify for this treatment, the required amendment or other modification generally must be made not later than at the next earliest church convention. However, the Secretary of the Treasury may prescribe an alternative time period within which the required amendment is to be made. In this regard, the Secretary is to take into account that church governing bodies typically meet at lengthy intervals. Of course, in no event is the permitted correction period for a church to be less than that allowed under present law (sec. 401(b)).

The conference agreement also follows the Senate amendment by providing that the tax rules for tax-sheltered annuities are to apply to church-maintained retirement income accounts that are defined contribution plans (sec. 414(i)). However, the conference agreement further provides that a church-maintained retirement income program in existence on August 13, 1982 will not be considered as failing to satisfy the requirements for a tax-sheltered annuity (sec. 403(b)) merely because the program is a defined benefit plan (sec. 414(j)). For this purpose, a church-maintained retirement income program is considered to be in existence on August 13, 1982, notwithstanding that after that date the program is amended, otherwise modified, or extended to benefit other employees. In addition, if a church-maintained retirement income program which is otherwise a defined benefit plan provides a benefit which is based, in part, on the balance of a separate account of an employee, the conferees intend that the separate account can qualify as a defined contribution plan for purposes of the rules relating to retirement income accounts.

The conferees intend that the assets of a retirement income account for the benefit of an employee or his beneficiaries may be commingled in a common fund made up of such accounts. However, that part of the common fund which equitably belongs to any account must be separately accounted for (i.e., it must be possible at all times to determine the account's interest in the fund), and cannot be used for, or diverted to, any purposes other than the exclusive benefit of such employee and beneficiaries. Provided those requirements are met, the assets of a retirement income account also may be commingled with the assets of a tax-qualified plan without adversely affecting the status of the account or the qualification of the plan.

The conferees also intend that the assets of a church plan (sec. 414(e)) may be commingled in a common fund with other amounts devoted exclusively to church purposes (for example, a fund maintained by a church pension board) if that part of the fund which equitably belongs to the plan is separately accounted for and cannot be used for or diverted to purposes other than for the exclusive benefit of employees and their beneficiaries. Of course, the reasonable costs of administering a retirement income account (including an account which is a part of a common fund) may be charged against the account. Such costs include the reasonable costs of administering a retirement income program of which the account is a part, including costs associated with informing employees and employers of the availability of the program.

5. State judicial retirement plans

Present law

Under present law, State or local government employees may defer compensation under an eligible State deferred compensation plan, subject to prescribed annual limits. If a plan of a State or local government is not an eligible plan, amounts under the plan are includible in an employee's income when there is no substantial risk of forfeiture.

House bill

No provision.

Senate amendment

The Senate amendment provides that participants in a qualified State judicial plan are not required to include benefits in gross income merely because there is no substantial risk that the benefits will be forfeited. The plan must be a mandatory retirement plan for State judges under which each contributes the same percentage of income and receives a retirement benefit based upon compensation paid to judges holding similar positions. The plan must have been continuously in existence since December 31, 1978, and must meet certain additional requirements. The provision applies to taxable years beginning after December 31, 1978.

Conference agreement

The conference agreement follows the Senate amendment.

6. Contribution for disabled employees

Present law

Under present law, contributions to a tax-qualified profit-sharing or other defined contributions to a tax-qualified profit-sharing or other defined contribution plan generally may not be made for an employee after the employee separates from the service of the employer.

House bill

No provision.

Senate amendment

The Senate amendment permits an employer to continue deductible contributions to a profit-sharing or other defined contribution plan for an employee (other than an officer, owner, or highly compensated individual) who is permanently and totally disabled provided that the contributions are nonforfeitable when made. For this purpose, a disabled employee's compensation is deemed equal to his annualized compensation prior to his becoming disabled. The provision applies to years beginning after December 31, 1981.

Conference agreement

The conference agreement follows the Senate amendment.

7. Participation in group trusts by governmental plans

Present law

Under present law, a group trust is exempt from tax only if each of the participating trusts is a qualified trust forming a part of a qualified pension, etc., plan or an IRA.

House bill

No provision.

Senate amendment

The Senate amendment provides that the tax-exempt status of a group trust will not be adversely affected merely because a participating trust is part of a governmental plan without regard to whether the governmental trust is a qualified trust or the governmental plan is a qualified plan. The provision applies to taxable years beginning after December 31, 1981.

Conference agreement

The conference agreement modifies the Senate amendment generally to permit all governmental retirement plans to participate in a tax-exempt group trust. Under the conference agreement, the tax-exempt status of a group trust will not be adversely affected merely because the trust accepts monies from (a) a retirement plan of a State or local government, whether or not the plan is a qualified plan and whether or not the assets are held in trust, or (b) any State or local governmental monies intended for use in satisfying an obligation of such State or local government to provide a retirement benefit under a governmental plan. Of course, any group trust in which a plan of a private employer participates will remain subject to the present-law rules relating to unrelated business taxable income (sec. 511 et seq.), notwithstanding that the trust includes a governmental plan.

E. Insurance Provisions

1. Reinsurance arrangements

Present law

Under present law, a ceding company and the reinsurer may elect to report a modified coinsurance transaction for tax purposes as if the assets relating to the risks reinsured were transferred to the reinsurer, as if the premium income for the reinsured policies and the investment income on the assets were received directly by the reinsurer, and also as if reserves to reflect liability for future claims were maintained by the reinsurer. However, no transfer of assets actually occurs. Through the use of modified coinsurance agreements and the payment of experience refunds by the reinsurer, some life insurance companies have used modified coinsurance to avoid or substantially reduce income taxes.

Under present law, a reinsurer (under either a modified coinsurance or a conventional coinsurance agreement between life insurance companies) is treated as having paid policyholder dividends to the extent it reimburses the ceding company for payment of such dividends.

House bill

No provision.

Senate amendment

The Senate amendment repeals the special elective provisions for modified coinsurance arrangements. Existing arrangements will be treated as terminated on January 1, 1982, and reinsurers will be permitted to pay any tax attributable to termination treatment in installments over a 3-year period. With respect to the reimbursement of policyholder dividends, the present law rule will continue for conventional coinsurance arrangements. With respect to other reinsurance arrangements, the Senate amendment denies any deduction (in computing taxable investment income) for interest paid on debt obligations issued by a ceding company in connection with such arrangements.[1] Also, the Secretary is granted authority to recharacterize items in connection with a reinsurance arrangement between related taxpayers in order to reflect the proper source and character of taxable income. Finally, pre-1982 modified coinsurance transactions are grandfathered except in the event of fraud.

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[1] It is the intention of the conferees that no inference is to be drawn from the inclusion of the limited specific rules (and exceptions) for debt-financed conventional coinsurance arrangements but not for other arrangements. In appropriate circumstances, the Internal Revenue Service may challenge other conventional coinsurance contracts on other grounds, e.g., the lack of economic substance of a transaction, the lack of a bona fide business purpose, or the fact that the principal purpose of the transaction is evasion of Federal income tax.

These provisions are effective as of January 1, 1982, except the special allocation authority for related party reinsurance contracts applies to contracts entered into after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment with certain modifications. One change makes it clear that increases in reserves attributable to the restoration of reserves to a ceding company under the modified coinsurance termination accounting rules do not qualify for the special deduction for 10 percent of the increases in reserves for nonparticipating contracts. A special election is provided under which certain ceding companies may revoke a section 820 election for modified coinsurance contracts entered into during 1980 or 1981 with an unrelated reinsurer. Only a company that had a loss from operations or was a "phase II negative" company for the year of the transaction is eligible to revoke the section 820 election. If revoked, the contract is treated as a modified coinsurance contract to which a section 820 election did not apply with respect to the reinsured company for all taxable years for which the contract is in force. A special transition rule is also provided to except interest paid in connection with a corporate restructuring transaction from the limitation imposed on interest incurred on debt issued for a coinsurance arrangement entered into early in 1982. The exception applies only if substantial cash principal payments were made prior to July 1, 1982, and the note is fully paid in cash before January 1, 1983.

The provisions relating to reimbursements are also revised so that policyholder dividends paid in connection with reinsured policies are treated as paid by the reinsured company rather than the reinsurer.

2. Policyholder dividends

Present law

Under present law, the deduction for policyholder dividends (and certain other special deductions) is limited to $250,000 plus the amount by which gain from operations (computed without regard to these deductions) exceeds taxable investment income.

House bill

No provision.

Senate amendment

The Senate amendment increases the $250,000 limit to $1 million. The limit must be allocated among members of an affiliated group of corporations. The limit is also phased out for larger companies (between $4 million and $8 million in dividends paid). Alternatively, at the annual election of the taxpayer, the amount of special deductions is limited to the sum of 100 percent of the policyholder dividends credited to qualified pension plans, the statutory amount of $1 million (subject to the affiliated group and phaseout rules), and 77½ percent of the policyholder dividends paid by mutual companies on other than pension business or 85 percent of policyholder dividends and the special deduction for nonparticipating contracts for stock companies.

These provisions apply for a 3-year period beginning with 1982 and ending with 1984.

Conference agreement

Generally, the conference agreement follows the Senate amendment. However, the provisions apply for a 2-year period (1982–1983) rather than a 3-year period.

3. Life insurance reserves and contract liabilities

Present law

Present law permits taxpayers to revalue life insurance reserves computed on a preliminary term basis to a net level premium basis. Under an approximate revaluation method, reserves for other than term insurance are generally increased by $21 per $1,000 insurance in force, less 2.1 percent of reserves under such contracts. Also, in computing reserves for certain contracts, taxpayers may reflect the future liability for interest (which may be guaranteed for more than one year) in excess of the assumed rate for such contracts.

Under present law, life insurance companies are deemed to allocate investment yield to pension contracts on the basis of the current earnings rate whether or not that rate exceeds the rate guaranteed under the contract. However, if the guaranteed rate of interest exceeds the current earnings rate, a taxpayer can allocate investment yield at the actual rate rather than the current earnings rate by removing life contingencies from the contracts.

For purposes of qualifying as a life insurance company for tax purposes, present law requires that more than 50 percent of a company's total reserves must consist of life insurance reserves. The Internal Revenue Service has several pending ruling requests concerning the reserve treatment of funds held under certain pension contracts that do not involve life contingencies (i.e., that do not contain permanent annuity purchase rate guarantees).

House bill

No provision.

Senate amendment

The Senate amendment revises the approximate revaluation formula for preliminary term reserves by reducing the revaluation from $21 to $19 per $1,000 of other than term insurance in force, for business written after March 31, 1982. In addition, no reserve deductions will be allowed for excess interest guaranteed beyond the close of a taxable year.

The Senate amendment provides that, beginning July 1, 1983, the policy or contract liability for group pension contracts, for purposes of determining the excludable policyholder share of investment yield, is limited to the amount of interest actually credited to the contracts. The intention is to eliminate the so-called "double-dip" available under present law with respect to these contracts.

Finally, the Senate amendment provides that, for any taxable year ending before January 1, 1985, life insurance company status for a company will not be changed by treating reserves for group pension contracts without permanent annuity purchase rate guarantees as not being insurance reserves.

The reduction for revaluing preliminary term reserves is effective for taxable years beginning after 1981 and before January 1, 1985, but only for business written after March 31, 1982. The limitation on computing reserves for guaranteed interest is effective for guarantees made after July 1, 1982, and before January 1, 1985. The limitation on interest credited to group pension contracts applies to periods beginning after July 1, 1983 and before January 1, 1985. The provision dealing with the status of a company as a life insurance company applies to taxable years ending before January 1, 1985.

Conference agreement

Generally, the conference agreement follows the Senate amendment. However, the reduction in the approximate revaluation formula for preliminary term reserves is made permanent rather than applying only for the 2-year period.

A transitional rule is provided for the rules disallowing excess interest guaranteed beyond the close of a taxable year for certain situations when the establishment of such reserves for taxable years beginning before January 1, 1982, did not result in any Federal income tax benefits. In these cases, the amount of such reserves may be recomputed by a taxpayer as of the beginning of the first taxable year beginning after December 31, 1981, to reflect the amount that would have been determined as of the close of the previous taxable year if the new limitation had been in effect. This recomputation would be taken into account for purposes of determining any increase or decrease in reserves for taxable years beginning after December 31, 1981. However, taxpayers taking advantage of this transition rule must compute such reserves in accordance with the new rule notwithstanding the fact that the interest rate guarantees were made prior to July 1, 1982.

Except for the permanent change relating to the revaluation of preliminary term reserves, the other provisions relating to life insurance reserves and contract liabilities will apply only during a period (1982-1983) rather than a 3-year period. The provisions relating to the allocation of investment yield to group pension contracts will apply as of January 1, 1983 (rather than July 1, 1983) during the 2-year period.

4. Menge formula

Present law

Under present law, a formula, commonly called the "Menge" formula, is used to compute the amount of adjusted life insurance reserves. Simply stated, the formula is a mechanical arithmetic adjustment used to compute adjusted life insurance reserves. The amount computed is then used in determining the policyholders' share of investment yield and accordingly affects the computation of a life insurance company's taxable investment income.

House bill

No provision.

Senate amendment

The Senate amendment provides a "geometric" Menge formula to compute adjusted life insurance reserves for purposes of allocating investment yield to policyholders. The provision applies to taxable years beginning after December 31, 1981, and before January 1, 1985.

Conference agreement

The conference agreement follows the Senate amendment. However, the provisions apply for a 2-year period (1982–1983) rather than a 3-year period.

5. Consolidated returns

Present law

Under present law, two or more affiliated domestic life insurance companies may elect to file a consolidated return. For reporting purposes, some taxpayers have taken the position that taxable income first is determined for each component member of the affiliated group and then consolidated by adding those separate company taxable incomes. This approach is sometimes referred to as the "bottom-line" method of consolidation. The ruling position of the Internal Revenue Service is that the taxable investment bases and the gain from operations bases first must be aggregated to arrive at consolidated group amounts and then these aggregate tax bases apply for the consolidated group. This approach is sometimes referred to as a "phase-by-phase" method of consolidation.

House bill

No provision.

Senate amendment

The Senate amendment provides that a "bottom-line" method of consolidation is allowed for determining consolidated life insurance company taxable income. Further, the Internal Revenue Service cannot disturb a bottom-line reporting position taken in a consolidated return filed for taxable years ending before 1982.

The provision applies to taxable years beginning after December 31, 1981, and before January 1, 1985. The grandfather protection applies to taxable years beginning before 1981 for returns (including amended returns) filed before July 1, 1982, and to taxable years beginning in 1981 for returns filed before September 16, 1982.

Conference agreement

Generally, the conference agreement follows the Senate amendment. However, the provisions apply for a 2-year period (1982–1983) rather than a 3-year period.

6. Allowance of deduction for excess interest

Present law

The Internal Revenue Service has ruled that excess interest credited by an insurance company with respect to certain deferred annuity contracts is a policyholder dividend subject to the statutory deduction limitation. Taxpayers have taken the position that excess interest is fully deductible as an increase in reserves for guaranteed contractual benefits.

House bill

No provision.

Senate amendment

The Senate amendment allows a deduction for 100 percent of the interest credited to qualified annuities if it is guaranteed in advance, at a fixed rate or in accordance with a formula, for a period of not less than 12 months. For purposes of this deduction an annuity contract is "qualified" if it is not a pension plan contract, involves life contingencies, is nonparticipating under State law, and provides for the payment of excess interest. A participating contract, meeting all other requirements, may also be treated as a qualified contract at the election of the taxpayer, but the interest deduction is limited to 92½ percent of total interest credited (i.e., assumed interest plus excess interest).

These provisions apply to taxable years beginning after December 31, 1981. Contracts with interest guarantees for less than 12 months and issued before January 1, 1983, are grandfathered if they are in compliance with the new provisions on January 1, 1983.

Conference agreement

The conference agreement generally follows the Senate amendment with certain technical and clarifying amendments. First, the interest guaranteed from a contract's original date of issue until the end of the taxable year qualifies for the 100 percent deduction even though it is guaranteed for less than 12 months. Second, with respect to participating contracts, 100 percent deduction is allowed for the permanently guaranteed rate of interest and 92½ percent for any interest credited in excess of the guaranteed rate. Third, contracts with interest guarantees for less than 12 months will be grandfathered with respect to moneys held on August 13, 1982, and any interest earned thereafter; contracts issued after August 13, 1982, and before January 1, 1983, must conform to the new provisions by the first contract anniversary date after January 1, 1983.

7. Amounts received under annuity contracts

Present law

Under present law, taxation of interest or other current earnings on a policyholder's investment in an annuity contract generally is deferred until annuity payments are received or amounts characterized as income are withdrawn. Amounts paid out before the annuity starting date are first a return of capital and are taxable (as ordinary income) only after investment in the contract is recovered. There is no tax penalty for withdrawals or surrenders before the annuity starting date or before a certain age.

House bill

No provision.

Senate amendment

The Senate amendment provides that amounts received before the annuity starting date will be treated first as withdrawals of income earned on investments to the extent of such income, the remainder being treated as a return of capital. Likewise, loans under the contract, or amounts received upon assignment or pledging of the contract, will be treated as amounts received under the contract. These provisions apply as of July 1, 1982, but do not apply to income amounts allocable to investments made before July 2, 1982, to endowment or life insurance contracts (except to the extent prescribed in regulations), or to contracts purchased under qualified pension plans.

In addition, the Senate amendment imposes a penalty on certain distributions from an annuity contract. The penalty will be equal to 10 percent of the amount includible in income, to the extent the amount is allocable to an investment made within 10 years of the receipt. However, the penalty will not apply to a distribution that is (1) made on or after the policyholder reaches age 59½; (2) made to a beneficiary on or after death of the policyholder; (3) attributable to the policyholder becoming disabled; (4) a payment under an annuity for life or at least 5 years; (5) from a qualified pension plan; or (6) allocable to an investment before July 2, 1982.

The penalty only applies to distributions made after December 31, 1982.

Conference agreement

The conference agreement generally follows the Senate amendment, but reduces the amount of the penalty to 5 percent and changes the effective date for the provisions to August 13, 1982 (except that the penalty still applies to distributions made after December 31, 1982).

Also, under the conference agreement, a replacement contract obtained in a tax-free exchange of contracts succeeds to the status of the surrendered contract for purposes of the new provisions. Such exchanges are subject to the new provisions in this Act for information reporting on pension plans and commercial annuity contracts.

8. Flexible premium contracts

Present law

Under present law, gross income does not include proceeds of a life insurance contract paid by reason of the death of the insured. In a private letter ruling, the Internal Revenue Service concluded that the entire amount paid upon death under a universal life insurance contract is excluded from gross income even though the death benefit may reflect a large cash fund and a relatively small amount of pure insurance protection. However, the Service is reconsidering this position.

House bill

No provision.

Senate amendment

The Senate amendment provides mandatory guidelines for determining whether a death benefit paid under a life insurance contract that provides for payment of one or more premiums not fixed by the insurer as to both timing and amount (a flexible premium life insurance contract) should be excluded from gross income. In addition to providing a life insurance benefit, such contracts can also provide benefits for guaranteed insurability, accidental death, family term coverage, or waiver of premium; they cannot provide any annuity benefits other than as settlement options.

The guidelines contain two tests which the contract must meet at all times in order to be considered life insurance thereunder. First, under a premium test, the sum of the premiums paid cannot exceed the single premium at issue (or sum of the level premiums) necessary to fund the death benefit of the contract and the charges for any qualified additional benefits. Second, under a death benefit test, the death benefit (without regard to any additional benefits) must never be less than specified percentages of the cash value of the contract. The amendment gives the Secretary discretion to allow corrections of excessive premium payments. It also allows 30 days after the close of the contract year to return excessive premium payments with interest to the policyholder and allows otherwise disqualifying premium payments if necessary to prevent terminations of the contract.

The amendment provisions apply to contracts issued before January 1, 1985. However, any contract issued before October 1, 1982, that complies with the new guidelines within one year after enactment shall be treated as being in compliance for all prior periods.

Conference agreement

The conference agreement generally follows the Senate amendment, but adds an alternative cash value test for purposes of meeting the flexible premium life insurance guidelines. Under this test, a flexible premium contract will provide life insurance for purposes of Code section 101 if, by the terms of the contract, the cash value will not at any time exceed the net single premium for the death benefit (without regard to any additional benefits) at such time. For purposes of this alternative test, the net single premium must be computed using the most recent mortality table, an assumed interest rate that is the greater of 4 percent or the minimum rate or rates guaranteed in the contract, and a maturity date of not earlier than age 95.

Because of difficulties in conforming certain existing contracts to the guidelines, the conference agreement modifies the transition rules concerning the assumed interest rates used in the guideline premium computations. In computing the net single premium for the alternative cash value test, the required assumed interest rate will be the greater of 3 percent or the minimum rate or rates guaranteed in the contract for contracts issued before July 1, 1983; a similar transition rule is adopted for purposes of the premium test and computing the guideline level premium, for contracts issued before January 1, 1983. Also, the conference agreement modifies the general transition rule to the Senate amendment and allows compliance within one year after enactment for any flexible premium contracts issued before January 1, 1983 (rather than October 1, 1982).

Also, the conference agreement clarifies that any flexible premium contract that is treated under State law as a single integrated life insurance contract and that satisfies these guidelines will be treated for Federal tax purposes as a single contract of life insurance and not as a contract that provides separable life insurance and annuity benefits.

Finally, the conferees agree to allow 60 days (rather than 30 days) to return excessive premium payments.

9. Indeterminate premium policies

Present law

In a private letter ruling, issued in June, 1982, the Internal Revenue Service held, among other things, that the excess of the maximum premium chargeable over the premium actually collected should be treated as a distribution of policyholder dividends which is paid back as a premium to the company.

House bill

No provision.

Senate amendment

The Senate amendment provides that, for taxable years beginning before 1982, amounts that could have been charged as a premium or mortality charge, but were not, will not be included in premium income.

Conference agreement

The conference agreement follows the Senate amendment.

10. Underpayments of 1982 estimated taxes

Present law

Under present law, a nondeductible penalty is imposed on underpayments of estimated taxes.

House bill

No provision.

Senate amendment

The Senate amendment provides that the underpayment penalty will not apply to underpayment periods ending before December 15, 1982, to the extent an underpayment is created or increased by the provisons of the bill affecting life insurance companies.

Conference agreement

The conference agreement follows the Senate amendment.

F. Employment Tax Provisions

1. Independent Cotractors

a. Alternative standards for determining classification of workers for employment tax purposes and extension of certain interim provisions

Present law

In general

Common law (i.e., nonstatutory) rules generally apply in determining whether particular workers are treated as employees or as independent contractors (self-employed persons) for Federal employment tax purposes. However, certain individuals are classified by the tax statute as employees for FICA (social security) tax purposes. These statutory FICA employees are certain agent-drivers or commission-drivers, full-time life insurance sales persons, home workers performing services on goods or materials, and full-time traveling or city sales persons.

Interim provisions relating to classification controversies

Section 530 of the Revenue Act of 1978 provided that taxpayers who had a reasonable basis for not treating workers as employees in the past could continue such treatment without incurring employment tax liabilities. This relief was available only if the taxpayer filed all Federal tax returns (including information returns) that are required to be filed with respect to workers whose status is at issue on a basis consistent with the taxpayer's treatment of the workers as independent contractors. Also, the 1978 Act prohibited the Treasury Department from issuing any regulation or revenue ruling that classifies individuals for purposes of employment taxes under interpretations of the common law.

The interim provisions of Section 530 of the Revenue Act of 1978 were extended, by subsequent legislation, through June 30, 1982.

Senate amendment

In general

The satisfaction of a safe-harbor test results in classification of a worker as an independent contractor for Federal employment tax purposes other than under the Railroad Retirement Tax Act. (A statutory FICA tax employee could be classified under the safe-harbor for income tax purposes.) The safe-harbor requirements, generally applicable to post-1982 services, relate to (1) control of hours worked, (2) place of business, (3) investment or income fluctuation, (4) written contract and notice of tax responsibilities, and (5) the filing of required returns. A special rule applies with respect to certain home-health care workers.

Interim provisions relating to classification controversies

The interim provisions (Section 530 of the Revenue Act of 1978) are extended through December 31, 1982.

Conference agreement

Statutory nonemployees.—The conference agreement does not include any safe-harbor test (or any special rule with respect to home-health care workers). The conference agreement establishes two categories of statutory nonemployees. Under this provision, sales persons who are licensed real estate agents, and individuals who are direct sellers, are treated for Federal income and employment tax purposes as self-employed persons where substantially all the remuneration paid for their services as real estate agents or direct sellers is directly related to sales or other output and where such services are performed pursuant to a written contract providing that they will not be treated as employees for Federal tax purposes. In defining direct sellers, the bill's reference to individuals engaged in the trade or business of selling or soliciting the sale of consumer products includes the activities of individuals who attempt to increase direct sales activities of their direct sellers and who realize remuneration dependent on the productivity of those direct sellers. These activities include providing motivation or encouragement, imparting skills, knowledge, or experience, or recruiting activities. Also, in defining qualified real estate agents, the bill's reference to sales persons who are licensed real estate agents includes the appraisal activities of licensed real estate agents in connection with real estate sales activities if such individuals realize remuneration dependent on sales or other output. This provision applies to services performed after 1982.

Interim provisions.—The conference agreement indefinitely extends the interim provisions (section 530 of the Revenue Act of 1978) from July 1, 1982, until such time as the Congress enacts legislation as to the classification of workers as independent contractors or employees. This provision does not prohibit implementation (e.g., through issuance of regulations or rulings) of the provision in the conference agreement relating to statutory nonemployees.

b. Reduction of certain employment tax liabilities where workers are reclassified as employees

Present law

If a worker reclassification occurs, the employer generally is responsible for all employment tax liabilities (income tax withholding, both the employer's and the employee's share of FICA taxes, and FUTA taxes) with respect to the reclassified workers. Federal income tax withholding assessments may be adjusted if the reclassified worker pays (or has paid) the proper amount of income tax. A FICA-SECA offset is authorized only if the reclassified worker is prevented from filing for a refund of the SECA tax paid in error.

House bill

No provision.

Senate amendment

The Senate amendment provides for reduced employment tax liability in certain reclassification cases.

Generally, an employer will be liable for 1.5 percent of wages (3.0 percent if no information returns were filed) if the employer erroneously treated the worker as a nonemployee for income tax purposes. If the employer erroneously treated the worker as a nonemployee for social security tax purposes, the employer will be liable for 20 percent of the worker's share of FICA tax that should have been withheld (40 percent if no information returns were filed). These reduced liabilities do not apply if the employer treats a worker as a nonemployee with intentional disregard of the law.

The Senate amendment is effective on enactment, but does not apply to assessments made before January 1, 1983.

Conference agreement

The conference agreement follows the Senate amendment.

c. Tax Court jurisdiction over certain employment tax issues

Present law

The U.S. Tax Court does not have jurisdiction over disputes involving Federal employment taxes.

House bill

No provision.

Senate amendment

The jurisdiction of the U.S. Tax Court is extended to include employment tax reclassification liabilities arising out of services performed after 1982.

Conference agreement

The conference agreement does not include the Senate amendment. The conferees understand that a taxpayer generally may challenge an employment tax assessment merely by paying the tax for one worker for one quarter, and then suing for a refund of that tax. Furthermore, the conferees understand that the Internal Revenue Service generally will forbear from active collection efforts while refund litigation is pending, if the government's interests are not jeopardized thereby.

2. Federal Unemployment Tax (FUTA) Provisions

a. FUTA tax rate

Present law

The Federal-State unemployment compensation system is financed by separate Federal and State payroll taxes on employers. Administrative funds are derived from the Federal payroll tax and benefits are paid mainly from State payroll taxes.

Under the Federal Unemployment Tax Act (FUTA), a payroll tax of 3.4 percent on the first $6,000 of wages is levied on employers who, in the current or last year, employed at least one person for 20 different weeks or had a quarterly payroll of at least $1,500. If a State's unemployment compensation program meets the requirements of Federal law, employers in the State receive a 2.7 percent credit against the 3.4 percent Federal tax. Thus, under current law, the standard net Federal tax rate in all States is 0.7 percent. (The tax rate is higher in certain States that have outstanding Federal unemployment loans.)

States also levy unemployment taxes on all covered employers in the State. These taxes finance regular State benefits and one-half the costs of extended benefits. The method and level of taxation varies considerably among the States. All States (except Puerto Rico) provide a system of experience rating under which State tax rates vary among employers according to the total amount of unemployment benefits that have recently been paid to former employees of each employer. In 1981, the estimated average State tax rate was 2.4 percent of taxable wages, ranging from 0.5 percent in Texas to 4.0 percent in Michigan. All States have a wage base of at least $6,000. Twenty-five States have a higher wage base, ranging from $6,600 to $14,000. In Puerto Rico, taxes are paid on total wages.

Sixty-five percent of the revenue raised by the Federal unemployment tax is allocated to the Employment Security Administration Account (ESAA) and 35 percent is allocated to the Extended Benefits Account (EUCA). Upon repayment of the Federal general revenue advances to EUCA, the 0.2 percent temporary tax will be eliminated and the allocation to EUCA will be reduced to 10 percent of the revenue raised by the Federal unemployment tax.

A State that has depleted its own unemployment funds may receive Federal loans as necessary to pay regular State benefits. States that borrow funds have 2 to 3 years to repay the loan, depending on the month the loan is received. If a State does not fully repay all loans within the 2 to 3 year period, employers in the State become subject to an annual reduction in the offset credit against the gross Federal unemployment tax rate of at least 0.3 percent. This means the net Federal tax rate, currently 0.7 percent, becomes subject to annual increases of at least 0.3 percent, up to a maximum of 3.4 percent, until sufficient revenue has been raised through such increases to repay the State's entire outstanding loan balance.

There are two potential credit reductions that are in addition to the annual 0.3 percent reduction. In the fourth year, in addition to another 0.3 percent reduction, employers in the State face a reduction equal to the amount that 2.7 percent exceeds the State's average tax rate on taxable wages in the calendar year to which the reduction applies. In the fifth year and thereafter, employers face a reduction, in addition to another 0.3 percent, equal to the higher of the amount of the additional fourth year reduction or the amount that the State's 5-year benefit cost rate exceeds the State's average tax rate on taxable wages in the calendar year to which the reduction applies. (The benefit-cost rate is benefits divided by taxable wages.)

Effective April 1, 1982, through December 31, 1987, States must pay interest on new Federal unemployment loans that are not repaid by the end of the fiscal year in which they are obtained. The interest rate is the same rate paid by the Federal Government on State reserves in the unemployment trust fund for the quarter ending December 31 of the preceding year, but not higher than 10 percent per annum. Interest payments are credited to the General Fund of the U.S. Treasury.

House bill

No provision.

Senate amendment

Effective January 1, 1983, the Senate amendment would increase the Federal unemployment tax wage base from $6,000 to $7,000. (This will require States, in order for employers to qualify for the 2.7 credit against the gross Federal tax rate, to have a State unemployment tax wage base of at least $7,000.)

The gross Federal unemployment tax rate would be increased from 3.4 to 3.5. Employers in States with approved State programs will continue to receive the 2.7 offset credit, so the standard net Federal tax would be 0.8 percent. This provision also is effective January 1, 1983.

Effective January 1, 1985, the Senate amendment would increase the gross Federal tax rate to 6.2 percent. This includes a permanent tax of 6.0 percent plus a temporary 0.2 percent that would remain in effect until all outstanding general revenue loans to the Federal Extended Unemployment Compensation Account (EUCA) have been repaid. The offset credit would increase to 5.4, so the net Federal tax rate would remain at 0.8 percent until the EUCA account has paid off all general revenue loans, when it would drop to 0.6 percent. The wage base remains at $7,000.

Conference agreement

The conference agreement follows the Senate amendment with the following modifications. States that, under State law in effect as of August 10, 1982, allow certain specified industries to pay a non-experience based State unemployment tax rate that is below 5.4 percent could provide for such industries to reach gradually the new 5.4 standard tax rate. Annual increases in the State unemployment tax rate for such industries could be limited to no less than 20 percent of the difference between the rate paid by an employer as of August 10, 1982 and 5.4 percent.

The allocation of Federal unemployment tax revenues among accounts in the Federal trust fund is modified to provide that 60 percent of the revenue raised by the 0.8 tax rate (or 0.48 percentage points) will be allocated to the Employment Security Administration Account (ESAA) and 40 percent (or 0.32 percentage points) to the Extended Benefits Account (EUCA). The Secretary will be required to make repayments to the General Fund of the Treasury from the EUCA account whenever he determines that the amount in the account exceeds the amount required to meet Federal extended benefit costs for the next 3 months. The conference agreement also provides, upon repayment of the Federal general revenue advances to EUCA (and elimination of the 0.2 percent tax), 90 percent of FUTA revenues will be allocated to ESSA and 10 percent of EUCA, as under current law.

The conference agreement allows States to make Federal unemployment loan repayments from State trust fund accounts in lieu of further reductions in the credit against the gross Federal unemployment tax rate, provided several requirements are met. First, the State account must have sufficient funds or sufficient income to enable it to repay an amount equal to at least the sum that the credit reduction would have generated plus any advances made to the State during the year. Second, after making this repayment, the State must retain enough funds in its account to pay all State benefits for the next 3 months (from November 1). Finally, the State must have made a change in its law, after the date of enactment of this bill, and after receiving the first advance, that has resulted in an increase in the solvency of its unemployment compensation system.

The conference agreement drops the additional credit reduction based on the State's previous 5-year benefit cost rate that begins in the fifth year a State is subject to annual reductions in the credit against the gross FUTA because of outstanding Federal unemployment loans. This amendment applies to a debtor State in any tax year, beginning after December 31, 1982, in which the State has taken no action during the 12-month period ending on September 30 which has reduced the solvency of the State unemployment trust fund.

Effective for interest due after December 31, 1982, the conference agreement permits States with high unemployment to reduce payments of interest on Federal unemployment loans to 25 percent of the amount due in any year, and thereby extend the payment of the total interest obligation over a 4-year period. (Interest would be charged on any deferred amount.) A State would be able to extend payment of interest due in any calendar year in which the State insured unemployment rate equaled or exceeded 7.5 percent during the first 6 months of the preceding calendar year.

b. Exclusion from FUTA of wages paid to certain students

Present law

Under current law, wages paid to a student under age 22 who is enrolled full-time in a work study or internship program are exempted from the Federal unemployment tax (FUTA) if the work performed is an integral part of the student's academic program.

House bill

The House provision exempts from FUTA tax any wages paid to a student enrolled full-time in a work-study or internship program, regardless of age, for work that is an integral part of the student's academic program, effective for services performed after the date of enactment.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House provision. In addition, for tax year 1983 only, the conferees agreed to exempt from FUTA, wages paid by certain summer camps to employees who are full-time students.

c. Extension of exclusion from FUTA of wages paid to certain alien farmworkers

Present law

Under the Immigration and Nationality Act, residents of foreign countries who do not intend to abandon such residency may be admitted to the United States to work for a temporary period of time during the peak agricultural crop seasons. Prior to 1982, wages paid to such alien farmworkers were excluded from Federal unemployment (FUTA) taxes.

House bill

The House provision extends for 2 years—from January 1, 1982, to January 1, 1984—the provision of prior law that excluded wages paid to certain alien farmworkers from FUTA taxes. The provision is effective upon date of enactment.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House provision.

3. Extension of Social Security hospital insurance taxes and Medicare coverage to Federal employees

Present law

Federal employees generally are not subject to social security hospital insurance taxes nor does their employment qualify them for Medicare coverage.

House bill

No provision.

Senate amendment

Federal employment would become subject to the hospital insurance portion of the FICA tax, effective January 1, 1983, and the newly covered Federal employment would be used in determining eligibility for protection under medicare part A (hospital insurance). A transitional provision would provide credit for additional hospital insurance quarters of coverage for certain Federal employees who have attained age 57 by 1983, and who otherwise would not qualify for medicare protection even though they have made hospital insurance tax contributions based on their Federal employment.

Conference agreement

The conference agreement follows the Senate amendment, with several clarifying and other changes, as follows: All Federal employment currently excluded from FICA taxes would be covered, except for certain services performed by penal inmates, medical interns and student nurses, and temporary emergency employment; hospital insurance quarters of coverage would be earned and credited in the same way as for other covered employment (i.e., specified amounts of covered earnings in a year would result in specified numbers of quarters of coverage); and the transitional provision, which would apply to Federal employees who perform service during and before January 1983, would give such employees credit toward medicare eligibility (up to the minimum amount required) for past Federal employment. Employees of States and localities, including the District of Columbia, would continue to be exempt from FICA taxes.

The conference agreement permits individuals who have worked for the Federal Government to obtain medicare benefits if they file and meet the insured status and other disability eligibility requirements of the social security disability cash benefits program, even though no such cash benefits would otherwise be payable. The medicare application would be treated as an application for disability benefits (for purposes of determining eligibility to medicare).

The Secretary of Health and Human Services and the Director of the Office of Personnel Management are required fully to inform Federal employees (particularly those who might be or become eligible for medicare benefits because of a disability) of the terms and conditions of medicare eligibility.

G. Excise Tax Provisions

1. Airport and airway taxes

Present law

There is a 5-percent tax on domestic air passenger tickets, the revenues from which go into the general fund. In addition, there is a 4-cents-per-gallon tax on gasoline used by noncommercial aviation and there are taxes on aircraft tires and tubes; the revenues from these taxes currently go into the Highway Trust Fund.

House bill

No provision.

However, H.R. 4800 as reported by the Committee on Ways and Means would have provided the following aviation excise tax rates for the period July 1, 1982–December 31, 1983: (1) 5-percent air passenger ticket tax; (2) 5-percent air freight waybill tax; (3) $5 per person international departure tax; (4) 12-cents-per-gallon tax on gasoline and nongasoline fuels used by noncommercial aviation; and (5) extension of the present taxes on aircraft tires and tubes. Revenues from these aviation excise taxes would have been transferred to the Airport and Airway Trust Fund for the period July 1, 1982–December 31, 1983, and the Airport and Airway Trust Fund statute would have been transferred to the Internal Revenue Code, effective July 1, 1982.

H.R. 4800 also would have made three other modifications to the application of the air passenger ticket tax:

(1) Effective July 1, 1982, the 6-hour layover rule would have been increased to 12 hours for purposes of determining whether the flight is treated as uninterrupted international travel subject only to the departure tax (i.e., not subject to the domestic ticket tax).

(2) The Secretary of the Treasury would have been granted the authority to waive the 225-mile zone rule if Canada or Mexico entered into a "qualified agreement" regarding the tax to be applied to persons traveling by air between the United States and that country with the objective of eliminating double taxation of travel between the countries or within the 225-mile zone.

(3) The requirement that the ticket fare and tax be shown by trip segments would have been repealed, effective from the date of enactment of the bill. The requirement for separately showing the total airfare and total ticket tax was retained.

In addition, H.R. 4800 would have repealed the present prohibition against charging aviation users for overtime costs associated with services provided by the U.S. Customs Service personnel during regularly scheduled hours on Sundays and holidays.

Senate amendment

Tax provisions

The Senate amendment makes the following permanent changes in aviation excise taxes: (1) increases the domestic air passenger ticket tax to 8 percent; (2) reimposes the prior 5-percent tax on air freight waybills; (3) reimposes the prior $3 per person international departure tax; (4) increases the tax on noncommercial aviation gasoline to 12 cents per gallon; (5) imposes a 14-cents-per-gallon tax on other noncommercial aviation fuels; (6) continues the tax on aircraft tires and tubes at present rates; and (7) provides an exemption from the fuels and air passenger ticket taxes for helicopters not utilizing Federal-aid airports or Federal airway facilities where used in (a) timber operations or (b) natural resource exploration or development. The tax changes are effective for tickets, waybills, and fuels purchased after August 31, 1982.

Trust fund provisions

Revenues from these aviation excise taxes are appropriated to the Airport and Airway Trust Fund, effective September 1, 1982. The Senate amendment also transfers the Airport and Airway Trust Fund statute to the Internal Revenue Code, effective September 1, 1982, and extends the trust fund expenditure authority on a permanent basis. The trust fund expenditure purposes are updated to include the Airport and Airway System Development Act of 1982 (as added by title IV of the Senate amendment).[1]

Tax termination provision

Title IV (sec. 406(e)) of the Senate amendment contains a provision which would terminate the aviation excise taxes going into the Trust Fund and the authority to make trust fund expenditures for airway improvement program costs (under sec. 407—airway facilities and equipment, research, engineering and development, and operations and maintenance expenses), if amounts obligated in any fiscal year for airport development are less than 85 percent of the amounts authorized. The termination of tax and trust fund spending provisions could be overridden by a joint resolution of the Congress.

Conference agreement

The conference agreement follows the Senate amendment with certain changes. The exemptions for helicopters from the fuels and air passenger ticket taxes are retained but only for those helicopters involved in timber operations and in hard mineral resource exploration and development.

The conference agreement does not include the provision of the Senate amendment for the automatic termination of the excise taxes that go into the trust fund and of the authorizations for the airway improvement program. Instead, the authority to make expenditures from the trust fund will expire after September 30, 1987, and the aviation excise taxes (and the transfer of tax revenues to the Airport and Airway Trust Fund) will terminate after December 31, 1987.

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[1] Title IV of the Senate amendment and title V of the conference agreement provides trust fund authorizations for fiscal years 1982-1987.

In addition, the conference agreement includes the three modifications from H.R. 4800 relating to the air passenger ticket tax, these modifications also being effective September 1, 1982.

2. Increase in cigarette excise taxes

Present law

A manufacturers excise tax equal to $4 per thousand (8 cents per pack) is imposed on small cigarettes (i.e., cigarettes weighing no more than three pounds per thousand). Generally, a tax equal to $8.40 per thousand is imposed on large cigarettes, except that higher rates apply to large cigarettes that exceed 6.5 inches in length.

House bill

No provision.

Senate amendment

The manufacturers excise taxes on small and large cigarettes are doubled effective for cigarettes removed after December 31, 1982, and before October 1, 1985. A floor stocks tax equal to the excess of the new tax rates over the pre-1983 rates is imposed on cigarettes held for sale on January 1, 1983, by any person other than a retailer. The floor stocks tax must be paid on or before January 18, 1983.

Conference agreement

The conference agreement follows the Senate amendment; however, the conferees desire to clarify their intent regarding the interpretation of two rules of the floor stocks tax applicable to cigarettes removed before January 1, 1983, and held for sale on that date.

The conferees intend that the exemption from the floor stocks tax for cigarettes held for sale by retailers apply only to cigarettes held at the location where they are normally sold to consumers. For example, cigarettes held for sale on the shelves of a retail store will be exempt as held by a retailer, but cigarettes held in warehouses or other similar facilities where retail consumers do not have regular access to them are not to be treated as held by a retailer.

The conferees further understand that financial hardship could result in some circumstances if payment of the entire floor stocks tax were required on or before January 18, 1983. It is the intent of the conferees that the Treasury Department exercise its present authority over establishment of the time and method for paying cigarette excise taxes to permit extensions of time of up to 30 days for payment of the floor stocks tax in circumstances where the taxpayer demonstrates that financial hardship would result from payment of the tax on the date otherwise prescribed.

3. Increase in telephone excise tax

Present law

The excise tax on local and long-distance telephone services and teletypewriter exchange service is 1 percent in calendar years 1982, 1983, and 1984. The tax is scheduled to terminate for bills rendered on or after January 1, 1985.

House bill

No provision.

Senate amendment

Under the Senate amendment, the tax rate is increased to 2 percent in calendar year 1983, 3 percent in 1984 and 1985, and 2 percent in years after 1985.

Conference agreement

The conference agreement increases the telephone excise tax to 3 percent for calendar years 1983–1985, and terminates the tax after 1985.

4. Windfall profit tax provisions

a. Windfall profit tax TAPS adjustment repeal

Present law

The windfall profit tax base price of Sadlerochit oil is adjusted upward by the amount by which the Trans-Alaska Pipeline System (TAPS) tariff falls below $6.26.

House bill

No provision.

Senate amendment

The TAPS adjustment is repealed effective for oil removed after December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment.

b. Windfall profit tax on Alaska Native Corporations

Present law

Under present law, certain domestic crude oil the producer of which is a native corporation "organized under" the Alaska Native Claims Settlement Act (as in effect on January 21, 1980) is exempt from the windfall profit tax.

House bill

No provision.

Senate amendment

The Senate amendment clarifies this exemption by providing that certain domestic crude oil, the producer of which is a corporation "organized pursuant to" the Alaska Native Claims Settlement Act (including a wholly owned subsidiary) is exempt Indian oil within the meaning of the windfall profit tax.

Conference agreement

The conference agreement follows the Senate amendment.

5. Expansion of Dingell-Johnson Fund taxes

Present law

A 10-percent manufacturers excise tax is imposed on the sale of fishing rods, creels and reels, and on artificial lures, baits, and flies by a manufacturer, producer, or importer. Revenues from the tax are appropriated for the Dingell-Johnson Fund program for transfer to the States to support fish restoration and management projects.

House bill

No provision.

Senate amendment

The Senate amendment expands the items of fishing equipment subject to the 10-percent tax and imposes a new 3-percent tax on certain recreational boats and boating accessories. Revenues from these taxes are appropriated to the Dingell-Johnson Fund.

The amendment also changes the time for paying the manufacturers excise taxes on fishing equipment and boats and boating equipment from monthly or semi-monthly to quarterly. Further, an amount equal to revenues from the tariffs on fishing equipment and on yachts and pleasure craft is appropriated for the Dingell-Johnson Fund program.

The Senate amendment is generally effective on October 1, 1982.

Conference agreement

The conference agreement does not include the Senate amendment.

H. Other Provisions

1. Exclusion from income of National Research Service Awards

Present law

National Research Service Awards made through 1981 are treated as excludable scholarships or fellowship grants.

House bill

No provision.

Senate amendment

The Senate amendment extends the Federal income tax exclusion for National Research Service Awards for two additional years. Thus, the exclusion applies to awards made in 1982 and in 1983.

Conference agreement

The conference agreement follows the Senate amendment.

2. Annual accrual accounting method for certain joint ventures

Present law

The taxable income from farming of a corporation (or a partnership of which a corporation is a partner) generally must be computed using the accrual method of accounting with the capitalization of preproductive period expenses (sec.447(a)). Preproductive period expenses are expenses (other than interest, taxes, or losses from casualty, drought, or disease) attributable to property having a crop of a yield that are incurred during the preproductive period of such property. The preproductive period for property is generally the period before the disposition of the property or the disposition of the first marketable crop or yield from the property.

This requirement, however, does not apply to subchapter S corporations, certain family corporations, or small corporations that meet a gross receipts test. Such corporations, and partnerships which have no other type of corporation as a partner, may use the cash method of accounting and may deduct preproductive period expenses when they are paid. The requirement to use the accrual method with the capitalization of preproductive period expenses also does not apply to the business of operating a nursery or a sod farm or the business of forestry or the growing of timber.

A special rule provides that certain corporations may use the "annual" accrual method of accounting (sec. 447(g)). Under the annual accrual method of accounting, preproductive period expenses are not capitalized, but are deducted currently. Corporations that qualify for this special rule are corporations that raise crops (such as sugar cane) which are harvested at least 12 months after planting. In addition, the corporation must have used the annual accrual method for the 10-year period ending with its first taxable year beginning after 1975, and must have continued to use such method for each taxable year after its first taxable year begininning after 1975.

In the case of a corporation that acquired substantially all the assets of a farming trade or business from another corporation in a transaction in which neither corporation recognized any gain or loss, the acquiring corporation is treated as having used the annual accural method for the period such method was used by the predecessor corporation to compute the taxable income from the acquired farming business.

House bill

No provision.

Senate amendment

A "qualified partnership" generally is treated the same as a corporation for purposes of the annual accrual accounting rules of secton 447(g). A qualified partnership is a partnership engaged in the trade or business of growing sugarcane, each of the partners of which is a corporation other than a subchapter S corporation or a personal holding company. The Senate amendment applies to taxable years beginning after December 31, 1981.

Conference agreement

The conference agreement generally follows the Senate amendment with certain clarifications. Under the conference agreement, a qualified partnership must be engaged in the trade or business of growing sugarcane and substantially all of the partnership activities must involve the growing of sugarcane. Growing sugarcane, however, does not have to be the principal activity of each of the partners.

3. Extension and revision of targeted jobs credit

Present law

The targeted jobs credit is available, on an elective basis, for hiring individuals from one or more of nine target groups. The credit is equal to 50 percent of the first $6,000 of wages paid for the first year of employment and 25 percent of the first $6,000 of wages paid for the second year of employment to a target group individual.

The credit is available for wages paid to eligible individuals who begin work for the employer before January 1, 1983.

An authorization of $30 million of appropriations is provided for fiscal year 1982 for the expenses of administering the certification system (including the performance of quality control reviews) and of providing publicity to employers.

An individual is a member of a targeted group if the individual is:

(1) an economically disadvantaged youth aged 16 through 19 participating in a cooperative education program,

(2) a recipient of money payments under a State or local general assistance program,

(3) an economically disadvantaged youth aged 18 through 24,

(4) a handicapped individual undergoing vocational rehabilitation,

(5) an economically disadvantaged Vietnam-era vetern,

(6) an SSI recipient,

(7) an economically disadvantaged ex-convict,

(8) an AFDC recipient or work incentive employee; or

(9) an involuntarily terminated CETA employee.

An individual may not be treated as a member of a targeted group unless the employer requests or receives a certification from the designated local agency before the day on which the individual begins work for the employer.

House bill

No provision.

Senate amendment

Extension of credit and authorization.—The credit is made available with respect to any member of a targeted group who begins work on or before December 31, 1985.

The $30 million authorization is extended to each of fiscal years 1983, 1984, and 1985.

Cooperative education students.—The requirement that cooperative education students must be economically disadvantged to be members of a targeted group is eliminated. The credit for cooperative education students is 30 percent of the first $3,000 of wages paid for the first year of employment and 15 percent of the first $3,000 of wages paid for the second year of employment.

General assistance recipients.—Recipents of non-cash, as well as cash, general assistance payments are members of a targeted group.

Summer youth.—A new targeted group is added, consisting of economically disadvantaged youths who are 16 or 17 years of age on the hiring date and who have not worked for the employer before the period for which the employer claims the credit. The credit for this group is 85 percent of up to $3,000 of wages paid for services attributable to any 90-day period between May 1 and September 15, effective for individuals beginning work for the employer after July 1, 1982.

Conference agreement

The conference agreement follows the Senate provision, with several modifications.

First, the credit is made available with respect to any member of a targeted group who begins work on or before December 31, 1984.

Second, the conference agreement does not contain the changes relating to cooperative education students. Under present law, for cooperative education students, the certification that an individual is a member of a targeted group is issued by the participating school. The determination of whether the student is a member of an economically disadvantaged family is made by the State employment security agency (SESA). However, the conferees intend that, whenever feasible, the SESA's exercise the authority they have under present law to contract with the schools to perform the initial eligibility determination as to whether the cooperative education students are economically disadvantaged. (The SESA's would continue to be responsible for the final determination of economically disadvantaged status, however.)

Third, the addition of summer youth group is made effective for individuals who begin work for the employer after April 30, 1983. A technical amendment is added to make clear that if an individual continues to work for an employer after having been a qualified summer youth employee, the certification of the individual as a member of another targeted group is to be determined on the basis of facts on the date on which the individual is certified as a member of the second targeted group rather than on the basis of the facts on the day the individual is hired by the employer.

Fourth, the target group consisting of individuals involuntarily terminated from CETA jobs will be terminated for individuals who begin work for the employer after December 31, 1982.

Fifth, the $30 million ceiling on the authorization of administrative funds will be eliminated, so that appropriations will be authorized for such sums as may be necessary in fiscal years 1983 and 1984. The conferees intend that some of these funds should be used to evaluate the effectiveness of the credit in improving the employment situation of the target groups.

Sixth, the Secretary of Labor will be required to submit annual quality control reports to the Congress reviewing the accuracy of the process by which the eligibility of individuals as members of targeted groups is determined.

Seventh, certifications will be valid if requested or received on or before the day the individual begins work for the employer.

4. Certain payments to foreign government officials or employees

Present law

Taxpayers cannot deduct payments to foreign government officials or employees if those payments would be illegal under U.S. law (if U.S. law applied).

House bill

No provision.

Senate amendment

Payments to foreign government officials or employees which are otherwise deductible would not be disallowed on grounds of illegality under U.S. law except payments made illegal by the Foreign Corrupt Practices Act. The provision would apply to payments made after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment but adds a technical amendment.

5. Debt management provisions

Present law

a. Rate of interest on U.S. savings bonds

The Secretary of the Treasury, with the approval of the President, may increase the investment yield on any U.S. savings bond above the current rate in any 6-month period by no more than 1 percentage point (annual rate, compounded semiannually).

b. Long-term U.S. bonds

Bonds are defined as obligations of the United States which have a maturity when issued that is longer than 10 years. The rate of interest that may be paid on a bond may not exceed 4¼ percent, except that up to $70 billion in outstanding bonds with rates of interest above 4¼ percent may be held by the public.

House bill

No provision.

Senate amendment

a. Rate of interest on U.S. savings bonds

The Secretary of the Treasury, with the approval of the President, is allowed to fix the investment yield on any U.S. savings bond. The Secretary also is authorized to provide for increases and decreases in the yield on any outstanding U.S. savings bond. With this authority, however, the Secretary may not decrease the yield on any bond below the minimum yield guaranteed at the time of its issuance for the period the bond is held.

This provision is effective on enactment.

b. Long-term U.S. bonds

The Senate amendment provides an additional $40 billion increase in the exception from the interest rate ceiling. This action raises the exception to $110 billion.

This provision is effective on enactment.

Conference agreement

a. Rate of interest on U.S. savings bonds

The conference agreement follows the Senate amendment.

b. Long-term U.S. bonds

The conference agreement follows the Senate amendment, with a modification requiring that all bonds issued under the additional exception must be issued in registered form.

6. Disclosure of Tax Returns

a. Disclosure of tax return information for nontax criminal investigation purposes

Present law

Overview

Tax returns and taxpayer return information (i.e., return information submitted to the Internal Revenue Service (IRS) by the taxpayer or his representative) may be disclosed for Federal nontax criminal investigation purposes only on the grant of an ex parte order by a Federal district court judge. Return information that is submitted to the IRS by someone other than the taxpayer or his representative may be secured on written request by certain officers and employees of the Federal government. The IRS, in certain circumstances, may disclose return information on its own initiative.

Disclosure pursuant to court order

Returns and taxpayer return information may be disclosed by the IRS to personnel of other Federal agencies for nontax criminal investigation purposes only on the grant of an ex parte order by a Federal district court judge.

Personnel to whom tax information may be disclosed

Tax information may be disclosed only to officers and employees of a Federal agency who are personally and directly engaged in the preparation for any administrative or judicial proceeding (or any investigation that may result in such a proceeding) pertaining to the enforcement of a Federal nontax criminal statute.

Individuals who may authorize an application for court-ordered disclosure

The following individuals may authorize the application for a court order: the head of a Federal agency, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General.

Court order standards

A Federal district court judge may grant an order for disclosure if the judge determines that:

(1) There is reasonable cause to believe, based upon information believed to be reliable, that a specific criminal act has been committed;

(2) There is reason to believe that the return or return information is probative evidence of a matter in issue related to the commission of such criminal act; and

(3) The information sought to be disclosed cannot reasonably be obtained from any other source, unless it is determined that, notwithstanding the reasonable availability of the information from another source, the return or return information sought constitutes the most probative evidence of a matter in issue relating to the commission of such criminal act.

Application for disclosure of return information other than taxpayer return information

The head of any Federal agency, the Attorney General, the Deputy Attorney General, or an Assistant Attorney General may obtain return information (other than taxpayer return information) by written request to the IRS. (This category of information is tax information that the IRS has received from someone other than the taxpayer under investigation or his representative.)

Contents of application

A request for return information (other than taxpayer return information) must set forth, among other information, the specific reason or reasons why the disclosure is or may be material to the proceeding or investigation.

Taxpayer identifying information

The name and address of a taxpayer may be disclosed, pursuant to written request, for use in a nontax criminal investigation.

Disclosure of return information (other than taxpayer return information) to apprise appropriate officials of possible criminal activities

Return information (other than taxpayer return information) that may constitute evidence of a violation of Federal criminal laws may be disclosed by the IRS to the extent necessary to apprise the head of the appropriate Federal agency charged with the responsibility of enforcement of such laws.

Under this provision, the taxpayer's identity may be disclosed if there is return information (other than taxpayer return information) that may constitute evidence of a violation of Federal criminal laws.

Use of tax information in administrative or judicial proceedings

In general, returns or return information disclosed by the IRS to a Federal agency may be entered into evidence in any administrative or judicial proceeding pertaining to enforcement of a nontax Federal criminal statute. A return or return information that was disclosed pursuant to a court order may be entered into evidence only if the court finds that it is probative of a matter in issue relevant in establishing the commission of a crime or the guilt of a party.

House bill

No provision. However, H.R. 6475 (as ordered reported by the Committee on Ways and Means) is identical to the Senate amendment.

Senate amendment

Overview

The primary changes made by the Senate amendment include: (1) the modification of the standards for the granting of an ex parte order for the disclosure of tax returns and return information and allowing Federal district court magistrates to issue those orders; (2) an expansion in the number of personnel who would be permitted to request disclosure; (3) new authority allowing court-ordered disclosure of return information for purposes of locating Federal fugitives from justice; and (4) new authority for the IRS to disclose return information, on its own initiative, in emergency circumstances.

The provisions take effect on the day after the date of enactment.

Disclosure pursuant to court order

The Senate amendment allows a Federal district court magistrate, as well as a Federal district court judge, to grant an ex parte order for the disclosure of returns or return information.

Personnel to whom tax information may be disclosed

The Senate amendment expands the category of personnel to whom disclosure can be made to include officers and employees of a Federal agency who are personally and directly engaged in any Federal grand jury proceeding pertaining to enforcement of a Federal nontax criminal statute.

Individuals who may authorize an application for court-ordered disclosure

The Senate amendment eliminates the authority of Federal agency heads (other than the Attorney General) to authorize disclosure applications. However, the number of individuals within the Department of Justice who can authorize applications is expanded to include: the Associate Attorney General, any United States Attorney, any special prosecutor, and any attorney in charge of a criminal division organized crime strike force.

Court order standards

Under the Senate amendment, a Federal district court judge or magistrate may grant an order for disclosure of tax returns or return information if the judge or magistrate determines that:

> (1) There is reasonable cause to believe, based upon information believed to be reliable, that a specific criminal act has been committed;
>
> (2) There is reasonable cause to believe that the return or return information is or may be relevant to a matter relating to the commission of such act; and
>
> (3) The return information is sought exclusively for use in a Federal criminal investigation or proceeding concerning such act, and the information sought to be disclosed cannot reasonably be obtained, under the circumstances, from another source.

With respect to the third standard, it would not be reasonable to obtain tax information from another source if, for example, the information cannot be obtained in an expeditious manner in a case where time is an essential factor, or if an attempt to obtain the information elsewhere would seriously impair a criminal investigation or proceeding.

Disclosure to locate Federal fugitives from justice

Persons who may authorize an application for court-ordered disclosure will be permitted also to authorize an application for the disclosure of returns and return information solely for the purpose of locating fugitives.

A Federal district court judge or magistrate may authorize a disclosure order if the judge or magistrate determines that:

(1) A Federal arrest warrant relating to the commission of a Federal felony offense has been issued for an individual who is a fugitive from justice;

(2) The return of such individual or return information with respect to such individual is sought exclusively for use in locating such individual; and

(3) There is reasonable cause to believe that such return or return information may be relevant in determining the location of such individual.

It is intended that this provision will be used to locate fugitives who are considered to be violent or dangerous or who pose a substantial threat to society.

Application for disclosure of return information other than taxpayer return information

The Senate amendment expands the number of individuals who can authorize a written request for disclosure to include the Inspector General of any Federal agency, the Associate Attorney General, the Director of the Federal Bureau of Investigation, the Administrator of the Drug Enforcement Administration, any United States Attorney, any special prosecutor, and any attorney in charge of a criminal division organized crime strike force.

Contents of application

A request for return information (other than taxpayer return information) must set forth, among other information, a showing of the specific reason or reasons why the disclosure is or may be relevant to (rather than material to) the proceeding or investigation.

Taxpayer identifying information

A taxpayer's social security number, as well as the taxpayer's name and address, may be disclosed, pursuant to written request, for use in a nontax criminal investigation.

It is intended that taxpayer identity information be treated as taxpayer return information unless return information (other than taxpayer identity information) is requested and disclosed pursuant to such written request.

Disclosure of return information to apprise appropriate officials of criminal activities or emergency circumstances

The IRS is provided with additional authority to disclose return information (including taxpayer return information) in certain emergency circumstances.

Specifically, under circumstances involving an imminent danger of death or physical injury to any individual, the IRS is permitted to disclose return information to the extent necessary to apprise appropriate officers or employees of any Federal or State law enforcement agency of such circumstances. Furthermore, under circumstances involving the imminent flight of any individual from Federal prosecution, the IRS may disclose return information to the extent necessary to apprise appropriate officers or employees of any Federal law enforcement agency of such circumstances.

Such disclosures will be subject to the safeguard and annual reporting requirements of section 6103(p). Moreover, it is intended the the IRS utilize its disclosure authority in an efficient and effective manner. The provision relating to imminent flight from Federal prosecution is intended to cover individuals who could be prosecuted for flight from prosecution, as a separate Federal offense, and circumstances where an individual has attempted to change identity or intends to flee from the country.

Use of tax information in judicial or administrative proceedings

The use of returns and return information in judicial or administrative proceedings not involving tax administration is expanded.

Specifically, this information may also be disclosed in any judicial or administrative proceeding pertaining to the enforcement of a civil forfeiture that is related to a nontax Federal criminal statute or to the extent required by court order pursuant to 18 U.S.C. sec. 3500 or rule 16 of the Federal Rules of Criminal Procedure.

Conference agreement

The conference agreement follows the Senate amendment. The purpose of these modifications to the disclosure law is to facilitate the disclosure of tax information for legitimate law enforcement needs while, at the same time, preserving the basic principle that a taxpayer's return should generally be treated as confidential and should be disclosed, in only a limited number of circumstances, where those law enforcement needs outweigh the need to preserve taxpayer confidentiality. In agreeing to these provisions, the conferees have fulfilled a commitment made by the conferees on the Economic Recovery Tax Act of 1981 to take appropriate legislative action in this area.

b. Civil damages for unauthorized disclosure of returns and return information

Present law

A person who knowingly or negligently discloses a return or return information with respect to a taxpayer, in violation of the disclosure restrictions, may be sued in a civil action for damages in a district court of the United States.

House bill

No provision. However, H.R. 6475 (as ordered reported by the Committee on Ways and Means) contains a provision that is identical to the Senate amendment.

Senate amendment

If a U.S. officer or employee knowingly or negligently discloses return information in violation of the disclosure restrictions, the wronged party will be permitted to bring a civil action for damages against the U.S. (rather than against the officer or employee). Of course, an officer or employee who makes a wrongful disclosure still will be subject to all administrative disciplinary actions as well as potential criminal sanctions.

The provision applies to disclosures made after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment.

c. Disclosure of returns and return information for use in certain audits by the General Accounting Office

Present law

The General Accounting Office currently has access to tax returns and return information for the purpose of conducting an audit of the Internal Revenue Service or the Bureau of Alcohol, Tobacco, and Firearms, and for the purpose of auditing the safeguards used by other agencies to safeguard returns and return information. However, before the GAO receives tax returns or return information in connection with an audit, it must notify the Joint Committee on Taxation of the audit. The Joint Committee may disapprove an audit by a vote of at least two-thirds of its members within 30 days of receipt of notice of the proposed audit.

In addition, the GAO is permitted access to returns and return information when it is acting as an agent for the Committee on Ways and Means, Committee on Finance, or Joint Committee on Taxation.

House bill

No provision. However, H.R. 6475 (as ordered reported by the Committee on Ways and Means) contains a provision that is identical to the Senate amendment.

Senate amendment

GAO access to tax returns and return information is expanded to include any returns or return information obtained by a Federal agency for use in any agency program or activity. This information will be open (upon written request) to officers and employees of the GAO, and only to the extent necessary in, auditing such program or activity. Furthermore, the GAO is permitted access to returns and return information that have not been obtained by a Federal agency in certain circumstances, provided that the agency is authorized to obtain the information for use in the program or activity that is the subject of the GAO audit. This "second-tier" access is limited to return information that may be disclosed under Code secs. 6103(l) or (m). The Internal Revenue Service may refuse to disclose tax information to the GAO if such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

The pre-audit notification procedures and Joint Committee veto authority of present law are retained. This notification should include (1) a description of the audit to be undertaken, including its scope and purpose; (2) an explanation of the use that will be made of tax information; and (3) assurance that in using tax information, and in formulating its recommendations which will result from the audit of programs that involve the use of tax information, the GAO will consider any potential impact on tax administration and taxpayer confidentiality.

In addition, within 90 days after the completion of any audit with respect to which the GAO had access to tax returns or return information, the GAO is required to notify the Joint Committee on Taxation of the completion. Such written notification will include (1) a description of the use of the returns and return information by the Federal agency involved; (2) such recommendations with respect to the use of returns and return information by the Federal agency as the Comptroller General deems appropriate; and (3) a statement of the impact of any such recommendations on the confidentiality of returns and return information and on tax administration. The GAO also is expected to notify the Joint Committee of any recommendations that will affect tax administration, directly or indirectly.

The present law authority for the GAO to gain access to tax information when it is acting as an agent for the Committee on Ways and Means, the Committee on Finance, or the Joint Committee on Taxation is retained. Moreover, the GAO may continue audit activity, which involves access to tax information, pursuant to any current agency designation, which is in process as of the date of enactment.

The provision takes effect on the day after the date of enactment.

Conference agreement

The conference agreement follows the Senate amendment. The conferees expect that before the GAO requests "second-tier" access (that is, access to return information that may be disclosed under Code secs. 6103 (l) or (m) but which has not been so disclosed), it will take into account the burdens that such access might impose upon the Internal Revenue Service.

7. Veterans organizations

Present law

A domestic post or organization of war veterans (or an auxiliary unit or society of, or a trust or foundation for such post or organization) is tax exempt if at least 75 percent of its members are "war veterans" and substantially all the other members are veterans or cadets, or are spouses, widows, or widowers of such individuals, and if no part of its net earnings inures to the benefit of any private individual.

House bill

No provision.

Senate amendment

The Senate amendment modifies the membership requirement to allow tax exemption for a veterans organization (which satisfies the other requirements of present law), if 75 percent of its members are past or present members of the U.S. Armed Forces (whether or not war veterans) and its remaining membership consists substantially of cadets or spouses, widows, or widowers of past or present members of the U.S. Armed Forces or of cadets.

The provision is effective on enactment.

Conference agreement

The conference agreement follows the Senate amendment, but with an additional amendment which also allows exemption for any veterans association founded before 1880, 75 percent of the members of which are past or present members of the U.S. Armed Forces, and the primary purpose of which is to provide insurance and other benefits to veterans and their dependents.

8. Amateur athletic organizations

Present law

Athletic organizations that teach youth or are affiliated with charitable organizations may qualify for tax exemption and eligibility to receive tax-deductible contributions if they meet the general requirements for charitable or educational organizations. Also, present law expressly provides that certain other athletic organizations may qualify for tax exemption and tax-deductible contributions if organized and operated exclusively to foster national or international amateur sports competition, but only if no part of the organization's activities involve the provision of athletic facilities or equipment and only if no part of the net earnings of the organization inure to the benefit of any private individual.

House bill

No provision.

Senate amendment

The Senate amendment allows tax-exempt status to amateur athletic organizations that conduct national or international competition in Olympic sports, or support and develop amateur athletes for such competition, whether or not the organization provides facilities or equipment to its members. The provision is effective as of October 5, 1976.

Conference agreement

The conference agreement generally follows the Senate amendment, with a modification to delete the restriction of the Senate bill that limits its application to sports listed on the program of the Olympic games or Pan-American games. Also, the conferees are concerned that some taxpayers may claim deductions for transfers to or for the use of amateur athletic organizations in cases where there is a direct benefit from the transfer to the taxpayer or other persons. The conferees intend that this provision does not modify the rules of existing tax law that a deduction is not allowed when there is a substantial, direct, personal benefit to the taxpayer or to any other person other than the amateur athletic organization.

9. Applicability of private foundation rules

Present law

Restrictions on business holdings

The Tax Reform Act of 1969 provided that private foundations generally may not own more than 20 percent of a business. Under transitional rules in the 1969 Act, foundations which, alone or in combination with related persons, owned more than 75 percent or alone owned more than 95 percent of businesses on May 26, 1969 have 15 or 20 years, respectively, to reduce their ownership interests to specified levels.

Charitable trusts

Under provisions enacted in the 1969 Act, trusts with solely charitable interests are generally subject to the private foundation rules, including the business holdings restrictions and the charitable distribution requirements.

House bill

No provision.

Senate amendment

Restrictions on business holdings

The Senate amendment provides that the Otto Bremer Foundation, the El Pamor Foundation, the Houston Endowment, the Public Welfare Foundation, and the Sand Springs Home may indefinitely retain certain business interests held on May 26, 1969, if the foundation meets certain conditions. Also, the Senate amendment provides that the Ahmanson Foundation will have an additional five years to meet the divestiture requirements with respect to certain stock held on May 26, 1969.

Charitable trusts

The Senate amendment provides that the New London Day Trust is not subject to the private foundation rules applicable to charitable trusts, effective for taxable years beginning after November 20, 1978.

Conference agreement

The conference agreement does not include the Senate amendment.

10. Clarification of tax status of certain members of religious orders

Present law

Present law exempts from the term "employment", for FICA tax purposes, service performed by a duly ordained, commissioned, or licensed minister of a church in the exercise of the ministry or by a member of a religious order in the exercise of duties required by such order. Likewise, "wages", for purposes of income tax withholding, does not include remuneration paid for similar services.

The Internal Revenue Service generally takes the position that a member of a religious order who is instructed by the order's superiors to obtain employment with a third party is an employee of the third party, not of the religious order, and must include the remuneration remitted to the order in gross income whether or not the member has taken a vow of poverty. Under this position, the remuneration is subject to FICA and income tax withholding.

House bill

No provision.

Senate amendment

Income derived from services of certain members of religious orders from salaries from the Public Health Service in a leprosarium is income of the religious organization, rather than income of the members. The provision, which benefits the Daughters of Charity, applies to services performed after September 30, 1977.

Conference agreement

The conference agreement does not include the Senate amendment.

11. Study of alternative tax systems

Present law

No specific provision.

House bill

No provision.

Senate amendment

The Secretary of the Treasury is instructed to conduct a study, to be submitted to the tax-writing committees within 6 months after the date of enactment, of the advisability of replacing only the Federal individual income tax, or both the Federal individual income tax and the Federal corporate income tax, with an alternative tax system, such as a simplified tax based on gross income, a consumption tax, and the current income tax system with a broadened base and lower rates.

Conference agreement

The conference agreement does not include the Senate amendment.

12. Study of monetary policy

Present law

No specific provision.

House bill

No provision.

Senate amendment

The Secretary of the Treasury is instructed to submit to the tax-writing committees, no later than 6 months after the date of enactment, a study of the effects on capital markets of using the growth of debt as the long-term target of monetary policy, and using total liquid assets as the interim target of monetary policy.

Conference agreement

The conference agreement does not include the Senate amendment.

13. New Jersey general revenue sharing allocation

Present law

Only taxes assessed and collected by a qualifying unit of government are counted toward the jurisdiction's tax effort under the general revenue sharing allocation.

House bill

No provision.

Senate amendment

The New Jersey Franchise and Gross Receipts Taxes shall be deemed an adjusted tax of units of local government for the purpose of allocating revenue sharing funds for the quarterly period beginning on October 1, 1982. This change will remain in effect for future quarterly payment periods only if New Jersey amends its Franchise and Gross Receipts Taxes statute to provide for local retention and collection.

This provision is effective for revenue sharing payments made with respect to the quarterly payment period in the quarter beginning October 1, 1982, and ending December 31, 1982.

Conference agreement

The conference agreement follows the Senate amendment.

14. Relief for the Jefferson County Mental Health Center, Lakewood, Colorado

Present law

Employees of a nonprofit organization are excluded from social security coverage unless the organization files with the Internal Revenue Service a certificate waiving its exemption from taxation.

House bill

No provision. However, H.R. 1635, as reported by the House Committee on the Judiciary on September 22, 1981, and passed by the House on October 6, 1981, is identical to the Senate amendment.

Senate amendment

The Senate amendment authorizes the payment of $50,000 to the Jefferson County Mental Health Center, Lakewood, Colorado, in full settlement of its claims against the United States for repayment of the $74,128 the Center refunded to its employees for individual social security contributions after the Internal Revenue Service erroneously advised the Center that the contributions had been incorrectly withheld. The provision is effective on enactment.

Conference agreement

The conference agreement follows the Senate amendment.

15. Award of reasonable litigation costs where taxpayer prevails and government position was unreasonable

Present law

a. Attorneys fees

A taxpayer who prevails in civil tax litigation in the Federal courts (other than the U.S. Tax Court) may be awarded reasonable attorneys fees and other litigation costs, unless the court finds that the position of the United States was substantially justified or that special circumstances make an award unjust.

b. Damages for delay in Tax Court

If a Tax Court proceeding has been instituted by the taxpayer merely for delay, the Court may award damages to the United States in an amount not to exceed $500.

House bill

a. Attorneys fees

General rule.—A taxpayer who prevails in civil tax litigation in the Federal courts, including the U.S Tax Court, may be awarded reasonable attorney fees and other litigation costs. The taxpayer may recover litigation costs only if the position of the United States in the case was unreasonable.

Dollar limitation on awards.—The maximum award is $50,000.

Third-party costs.—In litigation where the deductibility of contributions by a taxpayer to a charitable organization is the most significant issue, the organization (as well as the taxpayer) may recover costs incurred by it in the litigation if the taxpayer prevails, even though the charity is not a party to the action.

Effective date.—The attorneys fees provision applies to U.S. Tax Court cases begun after 1982, and to other Federal tax cases pending on, or begun after, October 1, 1981. The provision does not apply to cases begun after September 30, 1984.

b. Damages for delay in Tax Court

If U.S. Tax Court proceedings have been brought by a taxpayer primarily for delay, or if the taxpayer's position in a case is frivolous or groundless, the Court may award damages to the United States of up to $5,000, effective for Tax Court cases begun after 1981.

Senate amendment

No provision. However, a similar provision is included in H.R. 4717 as passed by the Senate.

a. Attorneys fees

General rule.—Generally the same as the House bill, except that the Senate provision provides explicitly that the taxpayer has the burden of establishing that the government's position was unreasonable.

Dollar limitation on awards.—The maximum award is $25,000. There is a special rule generally requiring the joinder or consolidation of multiple actions or actions involving the same taxpayer for the purpose of awarding attorney fees.

Third-party costs.—A taxpayer may recover costs for a third party incurred by that party on behalf of the taxpayer.

Effective date.—The attorneys fees provision applies to civil tax litigation, including U.S. Tax Court cases, begun after May 31, 1982. The provision does not apply to cases begun after May 31, 1987.

b. Damages for delay in Tax Court

Similar to the House bill, except that the maximum damages that may be awarded to the United States are $2,500 and the provision is effective for Tax Court cases begun after May 31, 1982.

Conference agreement

a. Attorneys fees

The conference agreement follows the Senate provision, except for effective dates. The provision applies to civil tax litigation, including U.S. Tax Court cases, begun on or after March 1, 1983. The provision does not apply to cases begun after December 31, 1985.

b. Damages for delay in Tax Court

The conference agreement follows the House bill (maximum $5,000 award), except for the effective date. The provision applies to Tax Court cases begun on or after January 1, 1983.

16. Personal holding companies

Present law

A corporation actively engaged in a lending or finance business is excluded from the personal holding company tax provisions if the corporation has qualifying business expenses equal to at least 15 percent of the first $500,000 of ordinary gross income from its lending or finance business, plus 5 percent of such ordinary gross income from $500,000 to $1 million.

The term "lending or finance business" is defined to include the business of making loans with maturities of not more than 60 months.

House bill

Effective for taxable years beginning after December 31, 1981, the House bill modifies the business expense test to require a lending or finance company to have qualifying business expenses equal to at least 15 percent of the first $500,000 of ordinary income from the lending or finance business, plus 5 percent of such ordinary gross income in excess of $500,000. Thus, 5 percent of ordinary gross income in excess of $1 million will be added to the qualifying business expense test of present law.

In addition, effective for taxable years beginning after December 31, 1980, the House bill increases the 60-month loan maturity limitation to 144 months, and the definition of a lending or finance business is amended to include the business of making loans in indefinite maturity credit transactions.

Senate amendment

No provision.

Conference agreement

The conference agreement follows the House bill.

17. Additional refunds relating to repeal of the excise tax on buses

Present law

The Energy Tax Act of 1978 repealed the prior law 10-percent manufacturers excise tax on buses effective after November 9, 1978. The Act also contained provisions effectively repealing the tax for buses sold after April 19, 1977 and before November 10, 1978, if a claim for refund was filed with the IRS and if the tax collected from ultimate purchasers was reimbursed before September 5, 1979.

House bill

The House bill extends the last date for reimbursing ultimate purchasers of buses to December 31, 1982, and permits the reimbursement to occur at the same time a refund from IRS is received. The provision applies only to taxpayers that filed a claim for refund before September 5, 1979.

Senate amendment

No provision. However, an identical provision is included in H.R. 4717 as passed by the Senate.

Conference agreement

The conference agreement follows the House bill.

18. Modification of rules as to acceleration of accrual of taxes

Present law

Under the accrual method of accounting, an expense generally is deductible for the taxable year in which all the events which determine the fact of the liability have occurred and the amount of the deduction can be determined with reasonable accuracy.

However, present law also provides that, if a taxing jurisdiction changes the date for imposing a deductible tax so that the tax would be deductible for an earlier period under the general rule, an accrual-basis taxpayer may not deduct the tax in the earlier period. Instead, the taxpayer may deduct the tax for the period that the tax otherwise would have been deductible as if the taxing jurisdiction had not accelerated the date for imposing the tax.

House bill

Under the House bill, an accrual-basis taxpayer may accrue a deduction for taxes on the liability date of the tax, even if that date has been accelerated by the taxing jurisdiction. However, the taxpayer is not allowed to take two deductions for taxes for a taxable year, and must account for the disallowed deduction by establishing a suspense account (which preserves the deduction until the level of tax is reduced or the taxpayer terminates its existence).

The provision applies to changes in tax liability dates that occur after the date of enactment. However, in the case of a State franchise tax based on income the assessment date of which has been changed, a taxpayer which first accrued such tax after the date of the change and which has consistently accrued the deduction for the tax on the new liability date could continue to accrue the deduction on the date used, without complying with the suspense account requirements under the provision.

Senate amendment

No provision.

Conference agreement

The conference agreement does not include the House provision.

19. Reassigning VHF television licenses

Present law

Present law does not contain any provisions on reassigning VHF licenses.

House bill

No provision.

Senate amendment

The Senate amendment adds a new section 331 to Title III of the Communications Act of 1934. New Jersey and Delaware are the only two States that do not have a commercial VHF television station. The amendment affirms the congressional intent that it is in the public interest for every State to have at least one VHF television station. In order to implement that intent, the amendment provides that, upon notice by any licensee in another State that it agrees to the reallocation of its channel to a community in a State in which there is no such channel, the Federal Communications Commission shall order the reallocation and issue a license to the licensee for such purpose.

This provision will remove impediments which currently discourage a licensee in a State which has more than one VHF television station from voluntarily moving to a State which has none. It is the intention of Congress that any current licensee which exercises the option of seeking the transfer of its license to an unserved State under the terms of this section will move its studio and offices, to and operate for the public benefit of the unserved State.

Conference agreement

The conference agreement follows the Senate amendment.

REVENUE EFFECTS OF TAX PROVISIONS OF H.R. 4961 AS AGREED TO BY THE CONFERENCE COMMITTEE

Table 1.—Summary of Estimated Revenue Effects of Tax Provisions of H.R. 4961 as Agreed to by the Conference Committee, Fiscal Years 1983–1987

[In millions of dollars]

Provision	1983	1984	1985	1986	1987
Individual income tax provisons	272	3,113	3,106	3,336	3,556
Business tax provisions	5,422	13,292	16,497	28,042	40,116
Compliance provisions	3,365	8,869	8,660	10,174	11,217
Pension provisions	194	780	870	970	1,058
Life insurance and annuities	1,942	2,155	2,920	3,138	3,370
Employment tax provisions	1,904	3,083	3,577	2,853	2,572
Excise tax provisions	2,798	4,009	4,702	2,054	1,472
Miscellaneous provisons	−38	−37	−34	−32	−30
Total, tax provisions	**15,859**	**35,264**	**40,298**	**50,535**	**63,331**
Revenue gain resulting from additional IRS enforcement personnel	2,100	2,400	2,400	1,300	600
Grand total, all provisions	**17,959**	**37,664**	**42,698**	**51,835**	**63,931**

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4961 as Agreed to by the Conference Committee, Fiscal Years 1983–1987

[In millions of dollars]

Provision	1983	1984	1985	1986	1987
Individual Income Tax provisions:					
Alternative minimum tax	(1)	659	701	741	729
Medical deduction	272	1,788	1,671	1,795	1,947
Ten percent casualty deduction floor		666	734	800	880
Total, individual tax provisions	**272**	**3,113**	**3,106**	**3,336**	**3,556**
Business Tax Provisions:					
Reduction in corporate preference items	515	936	948	918	995
Investment tax credit basis adjustment	362	1,374	2,658	4,109	5,579
Limit ITC to 85 percent of tax liability	152	259	213	178	164
1985–1986 ACRS changes			1,541	9,907	18,442
Construction period interest and taxes	555	1,179	1,206	1,084	819
Modifications to pre-ERTA and safe harbor leasing rules	1,036	2,649	4,252	5,496	7,000
Changes in taxation of foreign oil extraction income	200	438	508	569	621
Limit on possessions credit	201	428	473	516	559
Private purpose tax-exempt bonds	63	261	539	748	1,076
Mergers and acquisitions	427	749	959	1,014	1,064
Accounting for completed contracts	882	2,235	2,535	2,390	2,559
Original issue discount and coupon stripping provisions	163	310	465	629	808
Targeted jobs credit	−182	−551	−591	−271	−54
Accelerate corporate tax payments	1,048	3,025	791	755	484

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4961 as Agreed to by the Conference Committee, Fiscal Years 1983-1987—Continued

[In millions of dollars]

Provision	1983	1984	1985	1986	1987
Total, business tax provisions	**5,422**	**13,292**	**16,497**	**28,042**	**40,116**
Compliance Provisions:					
Withholding on interest and dividends	1,344	5,246	3,975	4,605	5,181
Other compliance provisions, including partnership audits and taxpayer safeguards [3]	2,021	3,623	4,685	5,569	6,036
Total, compliance provisions	**3,365**	**8,869**	**8,660**	**10,174**	**11,217**
Pension Provisions	**194**	**780**	**870**	**970**	**1,058**

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4961 as Agreed to by the Conference Committee, Fiscal Years 1983-1987—Continued

[In millions of dollars]

Provision	1983	1984	1985	1986	1987
Life Insurance and Annuities	**1,942**	**2,155**	**2,920**	**3,138**	**3,370**
Employment Tax Provisions:					
Independent contractors	−117	−107	−79	−85	−92
FUTA tax	1,404	2,353	2,729	1,872	1,501
Federal employees medicare tax	617	837	927	1,066	1,163
Total, employment tax provisions	**1,904**	**3,083**	**3,577**	**2,853**	**2,572**
Excise Tax Provisions:					
Airport and airway taxes [4]	817	962	1,089	1,216	1,357
Telephone tax [5]	616	1,073	1,600	730	...
Cigarette tax [6]	1,275	1,829	1,859	−34	−13
Repeal of Trans Alaska Pipeline System adjustment [7]	90	145	154	142	128
Alaska Native Claims Settlement Corp	...	...	...	...	...

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4961 as Agreed to by the Conference Committee, Fiscal Years 1983-1987—Continued

[In millions of dollars]

Provision	1983	1984	1985	1986	1987
Total, excise tax provisions	**2,798**	**4,009**	**4,702**	**2,054**	**1,472**
Miscellaneous Provisions:					
National Research Service Awards	−8	−7	−4	−2	(1)
Annual accounting for certain joint ventures					
Foreign Corrupt Practices Act provisions	−30	−30	−30	−30	−30
Disclosure of tax returns					
Veterans organizations	(2)	(2)	(2)	(2)	(2)
Amateur athletic organizations	(2)	(2)	(2)	(2)	(2)
Relief for the Jefferson County Mental Health Center	(8)				
Award of certain litigation costs	(9)	(9)	(9)	(9)	(9)
Treatment of certain lending or finance businesses for purposes of the tax on personal holding companies	(2)	(2)	(2)	(2)	(2)
Additional refunds relating to repeal of the excise tax on buses	(1)	(1)	(1)	(1)	(1)
Total, miscellaneous provisions	**−38**	**−37**	**−34**	**−32**	**−30**
Total, tax provisions	**15,859**	**35,264**	**40,298**	**50,535**	**63,331**
Revenue gain resulting from additional IRS enforcement personnel	2,100	2,400	2,400	1,300	600

Table 2.—Estimated Revenue Effects of Tax Provisions of H.R. 4961 as Agreed to by the Conference Committee, Fiscal Years 1983-1987—Continued

[In millions of dollars]

Provision	1983	1984	1985	1986	1987
Grand total, all tax provisions	**17,959**	**37,664**	**42,698**	**51,835**	**63,931**

[1] Negligible.

[2] Loss of less than $5 million.

[3] Additional gains in budget receipts are expected from the Administration's proposal to increase IRS personnel in taxpayer compliance enforcement activities: $2.1 billion in fiscal year 1983, $2.4 billion in 1984, $2.4 billion in 1985, $1.3 billion in 1986, and $0.6 billion in 1987.

[4] The figures represent net increases, after accounting for lower income tax receipts. Additional revenues from aviation excise taxes, resulting from this bill before taking account of the income tax offset are estimated at $1,089 million in 1983, $1,283 million in 1984, $1,452 million in 1985, $1,621 million in 1986, and $1,809 million in 1987.

[5] The figures represent net increases, after accounting for lower income tax receipts. Increases in general fund receipts from this tax before taking account of the income tax offset are estimated at $821 million in fiscal year 1983, $1,431 million in 1984, $2,133 million in 1985, and $973 million in 1986.

[6] The figures represent net increases, after accounting for lower income tax receipts. Increases in general fund receipts from this tax before taking account of the income tax offset are estimated at $1,700 million in fiscal year 1983, $2,439 million in 1984, $2,479 million in 1985.

[7] The figures represent net increases, after accounting for lower income tax receipts. Increases in general fund receipts from this tax before taking account of the income tax offset are estimated at $139 million in fiscal year 1983, $260 million in 1984, $285 million in 1985, $267 million in 1986, and $241 million in 1987.

[8] Increases outlays by $50,000.

PART THREE

CONTENTS OF AIRPORT AND AIRWAY IMPROVEMENT PROVISIONS

TITLE V

Page

Airport and airway improvement provisions 699
1. Short title 699
2. Declaration of policy 699
3. Definitions 700
4. National plan of integrated airport systems 702
5. Navigation aids 703
6. Airport improvement program 703
7. Airway improvement program 704
8. Apportionment of funds 708
9. Minimum funding 709
10. Use of apportioned funds 710
11. Project grants: application; approval 710
12. U.S. share of projects costs 711
13. Sponsorship requirements for project grants 711
14. Block grants to States 713
15. Acceptance of certification; consultation 713
16. Grant agreements 713
17. Project costs 714
18. Payments under grant agreements 715
19. Performance of construction work 715
20. Use of Government-owned lands 715
21. False statements 716
22. Access to records 716
23. General powers 716
24. Civil rights 717
25. Judicial enforcement 717
26. Voluntary withdrawal from program 717
27. Waiver of obligations 718
28. Repeals; effective date; savings provisions; separability 718
29. Report to Congress on Trust Fund 718
30. Standards for runway friction 718
31. Equal aeronautical access 719
32. Conforming amendments 719
33. Security screening in foreign air commerce 719
34. Safety certification of airports 719

PART THREE—Continued

Page

35. Part-time operation of flight service stations 720
36. Congressional committees 720
37. Contracting authority 720
38. Study of airport access 721
39. K–9 teams 721
40. Release of certain deed restictions 721
41. Continuation of certain certificates 722
42. State taxation 722

AIRPORT AND AIRWAY IMPROVEMENT

Title IV of the Senate amendment to H.R. 4961 consisted of the Airport and Airway System Development Act of 1982. The House bill contained no comparable provisions. The joint explanatory statement that follows contains a description of the Senate provisions and the conference substitute for each provision.

1. SHORT TITLE

Senate amendment:

Provides that the act may be cited as the "Airport and Airway System Development Act of 1982".

Conference substitute:

Provides that the Act may be cited as the "Airport and Airway Improvement Act of 1982".

2. DECLARATION OF POLICY

Senate amendment:

Sets forth as policies and findings: that the safe operation of the airport and airway system will continue to be the highest aviation priority; that the continuation of airport and airway improvement programs, including both development and planning activities, and more effective management and utilization of the Nation's airport and airway system are required to meet current and projected growth in aviation; that this Act should be administered so as to provide adequate navigation aids and airport facilities, including special emphasis on the development of reliever airports, for points where scheduled commercial air service is provided; that aviation facilities should be built and operated with due regard to providing substantial relief from current and projected noise impacts on nearby communities; that airports which have the ability to finance their capital and operating needs without Federal assistance should be encouraged to voluntarily withdraw from eligibility for such assistance; and that the Federal administrative requirements placed upon airport sponsors can be reduced and simplified through the use of single project applications to cover all airport improvement projects.

Conference substitute:

Same as the Senate except for deletion of the provision encouraging airports to finance their needs without Federal assistance and the addition of the following: a statement regarding the providing of reliever heliports; a qualification of the goal of installing precision approach systems by reference to available funds and other safety needs; and a statement that it is in the national interest to develop in metropolitan areas an integrated system of airports. In addition, the conference substitute includes a more detailed statement to encourage and promote multimodal transportation planning.

3. DEFINITIONS

Senate amendment:

The Senate amendment contains many of the definitions contained in the Airport and Airway Development Act of 1970 with some technical changes to conform to the present bill. The following are new or modified definitions:

(1) "airport development": in addition to items covered in the existing law, this definition would make the preparation of plans and specifications, including field investigations incidental thereto, eligible; broaden the definition of airport development for environmental, safety or security reasons; make newly eligible the acquisition or installation of safety or security equipment which the Secretary approves for use, even if the use of such equipment is not required by the Secretary; make the acquisition or installation of aviation-related weather reporting equipment eligible; and set forth items eligible as airport development which are related to improving noise compatibility at public-use airports (these items are eligible under the present act; however, this provision would newly provide that the elements of airport noise compatibility programs approved by the Secretary are eligible as airport development).

(2) "airport noise compatibility planning" and "airport noise compatibility program": these terms are taken from the Aviation Safety and Noise Abatement Act of 1979 and are defined here for inclusion in the definition of airport development in this bill.

(3) "airport planning" would be defined as such planning as the Secretary may prescribe by regulation, and specifically includes airport system planning and airport noise compatibility planning.

(4) "airport system planning" in the present Act would be modified to make explicit several concepts inherent in the present definition. The words "initial as well as continuing" have been inserted to clarify that airport system planning is a continuous process. The definition would also make eligible for funding as airport system planning a State's development of certain airport construction and development standards.

(5) "block grant", "block grant supplement", "applicant State", "participating State", and "State development report" are defined for purposes of the block grant program in the Senate amendment.

(6) "commercial service airport": any airport which the Secretary determines to either: (A) enplane 2,500 or more passengers annually and receive scheduled passenger service of aircraft; or (B) enplane 10,000 or more passengers annually, is a commercial service airport.

(7) "eligible airport" is defined with reference to the provision of the Senate amendment relating to voluntary withdrawal from the program.

(8) "passengers enplaned" means revenue passengers enplaned in the United States who are flying between domestic, territorial, or

international points via aircraft, whether scheduled or nonscheduled.

(9) "primary airport" is a new term meaning any "commercial service airport" determined by the Secretary to have enplaned .01 percent or more of the total number of passengers enplaned annually, both scheduled and nonscheduled, at all commercial service airports.

(10) "project" means a project or separate projects submitted together for the accomplishment of airport development or airport planning, including the combined submission of all projects which are to be undertaken at an airport in a fiscal year.

(11) "public-use" airport is a new term meaning any public airport or any reliever airport whether publicly or privately owned, which is or is to be available for use by the public. This bill would provide that airport development and planning funds may be distributed for use at public-use airports.

(12) "reliever airport" is defined as an airport designated by the Secretary as having the function of relieving congestion at a "primary airport".

(13) "sponsor" is any public agency which individually or jointly with other public agencies, submits to the Secretary, in accordance with this Act, an application for financial assistance for a public airport. A "sponsor" can also be any private owner of a public-use airport which submits to the Secretary, in accordance with this Act, an application for financial assistance for a public-use reliever airport. A sponsor can also be a participating State.

(14) "State" means a State of the United States, the District of Columbia, or the Commonwealth of Puerto Rico.

Conference substitute

Same as the Senate amendments, except as follows:

(1) Airport Development: The conference substitute includes within this definition the acquisition of equipment to measure runway surface friction.

(2) Definitions and references relating to noise abatement are deleted, as the noise compatibility programs are to be eligible for fiscal year 1983 and thereafter only under the Aviation Safety and Noise Abatement Act of 1979 (although the funding will continue to be provided under the airport improvement program in this bill). For fiscal year 1982, a special provision is added to include the noise related programs from the Senate amendment within the definitions of airport development, so that applicants can apply for noise projects under this bill as well as under ASNA for fiscal year 1982.

(3) The definitions relating to block grants and eligible airports are deleted because of the deletion of the substantive provisions to which these terms refer.

(4) "commercial service airport" is modified to delete the alternative test of 10,000 enplanements.

(5) "public-use airport" is modified to add privately-owned airports whih annually enplane 2,500 passengers and receive scheduled service.

(6) "reliever airport" is modified to add the condition that to be a reliever an airport must provide more general aviation access.

(7) "State" is modified to include all the insular areas.

4. NATIONAL PLAN OF INTEGRATED AIRPORT SYSTEMS

Senate amendment:

Provides that the Secretary shall review and revise as necessary the existing national airport system plan.

Provides that in revising the National Airport System Plan, the Secretary shall consult to the extent feasible with other Federal and public agencies and with the aviation community.

Provides that the Department of Defense shall make domestic military airports available for civil use to the maximum extent feasible. The Comptroller General is to report to Congress within 180 days on the feasibility of joint civil and military use of military airports, including cost estimates. Within one year the Secretaries of Defense and Transportation are to submit a plan for joint civil and military use.

Conference substitute:

Same as the Senate amendment with respect to the issue of joint use of military airports.

The Conference substitute continues the requirement of a system plan for the national air transportation system. The plan shall include the type and estimated cost of eligible airport development necessary to provide a safe, efficient and integrated system of public use airports to meet the needs of civil aeronautics, the national defense, and the postal service. Airport development identified by the plan shall not be limited to the requirements of any classes or categories of public use airports and in reviewing and revising the plan the Secretary shall consider the needs of and consult with all segments of civil aviation.

The Conference substitute also clarifies that the plan should provide for the development of an integrated system of public use airports. To emphasize the importance of this concept, the plan is designated as the National Plan of Integrated Airport Systems.

The concept of Integrated Airport Systems has special application to the metropolitan areas of the country. The basic objective of the Integrated Airport System is to develop a master plan for airport site selection based on the airspace capacity of a given area.

The cornerstone of the Integrated Airport System concept is its emphasis on the development and improvement of reliever airports. These airports not only relieve congestion in our major metropolitan areas by attracting air traffic away from the busier air carrier facilities, but also provide badly needed access to these areas for general aviation. Implementation of a viable reliever system is therefore critically needed to increase the safety and capacity of our national airport system while giving full recognition to the importance of general aviation for the economic development of these areas.

Because the conferees recognize the importance of improving our reliever system without further delay, the Conference Report sets aside a substantial portion of ADAP funds to accomplish these objectives. Accordingly, the Conference Report would fund reliever airports at a minimum of 10 percent of the total funds made available under the ADAP program—an amount which could result in reliever funding at an average of approximately $80 million per year over the 6-year period covered by the legislation.

It is critical that we implement the Integrated Airport System in metropolitan areas at the earliest possible date. The same concepts can be applied to rural areas throughout the U.S. where a number of communities in need of air transportation and airport services could establish an airport authority or by joint powers agreement adopt and implement the integrated airports concept.

The Conference Report includes a number of provisions to ensure that high priority is given to the integrated airport concept. As has been discussed, the National Airport System Plan will now focus on the integrated airport concept, and there will be guaranteed minimum funding for integrated airport system planning. In addition, the policy statements of the Act have been amended to emphasize the importance of this concept and to provide that in establishing priorities for the distribution of funds, the Secretary may give priority to projects that are consistent with integrated airport system plans.[1]

5. NAVIGATION AIDS

Senate amendment:

Under the bill, the Secretary may require a sponsor, as a condition to receiving the grant, to perform certain site preparation work associated with the acquisition, establishment, or improvement of air navigation facilities under section 307(b) of the Federal Aviation Act of 1958 (49 U.S.C. 1348(b)). This section clarifies that the cost of any such work is to be paid for from appropriated funds made available to the Secretary for airway facilities and equipment.

Conference substitute:

Same as Senate amendment.

6. AIRPORT IMPROVEMENT PROGRAM

Senate amendment:

Authorizes the Secretary to make grants for airport development and planning in aggregate amounts of $450 million for fiscal year 1982; $1,050 million for fiscal years prior to October 1, 1983; $1,843.5 million for the fiscal years prior to October 1, 1984; $2,755.5 million for the fiscal years prior to October 1, 1985; $3,772.5 million for the fiscal years prior to October 1, 1986; and $4,789.7 million for the fiscal years prior to October 1, 1987. This insures that authorizations which are not appropriated from the Trust Fund in any given fiscal year are carried forward.

The Secretary is precluded from incurring obligations for airport development after September 30, 1987, except for apportioned funds which remain available after such date.

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[1] For a further discussion of these important concepts, see the remarks of Cong. Don Clausen as printed in the August 9, 1967 Congressional Record, beginning on p. 10234.

The amendment precludes obligation for airport development at any airport that has elected not to receive such Federal assistance under the bill. It also spells out the guidelines for obligations incurred by the Secretary for airport development at privately owned reliever airports.

Finally, the Senate amendment provides for a termination of aviation taxes and the authority of the Secretary to carry out certain programs if the amount made available for airport development grants is less than 85 percent of authorized levels.

Conference substitute:

Same as the Senate except that there is no provision for airports electing not to receive Federal assistance. Also the provision that the Secretary receive assurances that a privately owned reliever or commercial service airport receiving funds continue to function as a public-use airport during the economic life of the project is modified to require a minimum of ten years for that assurance. The provision relating to termination of taxes was referred to the conferees on the tax portion of the bill.

7. AIRWAY IMPROVEMENT PROGRAM

Senate amendment:

Authorizes appropriations from the Trust Fund for the procurement of air navigational facilities; research, engineering and development activities; payment of a portion of the operation and maintenance costs of the national airspace system; and other activities related to airway improvement.

The authorization for each fiscal year for the acquisition, establishment, and improvement of air navigation facilities remain available in future fiscal years to the extent that appropriations for that fiscal year are less than the authorization. The amounts authorized are $261,000,000 for fiscal year 1982; $725,000,000 for fiscal year 1983 (an aggregate amount of $986,000,000 for fiscal years 1982 and 1983); $1,393,000,000 for fiscal year 1984 (an aggregate amount of $2,379,000,000 for fiscal years 1982 through 1984); $1,407,000,000 for fiscal year 1985 (an aggregate amount of $3,786,000,000 for fiscal years 1982 through 1985); $1,377,000,000 for fiscal year 1986 (an aggregate amount of $5,163,000,000 for fiscal years 1982 through 1986); and $1,164,000,000 for fiscal year 1987 (an aggregate amount of $6,327,000,000 for fiscal years 1982 through 1987).

For research, engineering and development, and demonstration projects the authorizations are $72,000,000 for fiscal year 1982; $134,000,000 for fiscal year 1983; $286,000,000 for fiscal year 1984; $269,000,000 for fiscal year 1985; $215,000,000 for fiscal year 1986; and $193,000,000 for fiscal year 1987. The amounts appropriated are to remain available until expended.

The Senate amendment provides that all FAA operating expenses may be funded from the Trust Fund, and the authorizations from the Trust Fund for operations and maintenance are as follows: $800,000,000 for fiscal year 1982; $1,559,000,000 for fiscal year 1983; $1,355,000,000 for fiscal year 1984; $1,363,000,000 for fiscal year 1985; $1,388,000,000 for fiscal year 1986; and $1,444,000,000 for fiscal year 1987. These funds are mandatorily reduced by a like amount in the succeeding fiscal year to any reductions made in the minimum authorized levels for ADAP or F&E in any fiscal year covered by the bill. From these funds, the Secretary is authorized to reimburse the National Oceanic and Atmospheric Administration for the cost of providing the FAA with weather reporting services. These amounts are limited to the following: $26,700,000 for fiscal year 1983, $28,569,000 for fiscal year 1984, $30,569,000 for fiscal year 1985, $32,709,000 for fiscal year 1986, and $34,998,000 for fiscal year 1987.

In addition the Senate amendment contains provisions similar to those in existing law establishing the priority of the Trust Fund for airport and airway programs, preserving sufficient amounts in the Trust Fund for such programs, and prohibiting the use of the Trust Fund for administrative expenses, except as otherwise provided in the bill.

Finally the Senate amendment places a cap on the total amount of Trust Fund moneys which may be expended in a fiscal year of 75 percent of the FAA's total expenditures for that year.

Conference substitute:

Same as Senate, with the following exceptions:

Of the amounts authorized for research, engineering and development, and demonstration projects, a specified maximum amount is authorized for facilities, engineering and development.

Only direct costs to flight check, operate, and maintain air navigation facilities are included as eligible operating expenses. The amount authorized from the Trust Fund for operations and maintenance is $800,000,000 for fiscal year 1982 and for later years is a multiple of the amount actually made available for airport development, airport planning, and noise abatement. The multiple is 2.44 for fiscal year 1983, 1.57 for fiscal year 1984, 1.39 for fiscal year 1985, 1.28 for fiscal year 1986, and 1.34 for fiscal year 1987.

The amount authorized from the Trust Fund for operations and maintenance for any fiscal year is reduced by twice the amount that authorizations exceed the appropriations for facilities and equipment for that fiscal year.

The 75 percent overall cap in the Senate amendment is not included in the bill.

The Conference Substitute's authorization levels for Facilities and Equipment reflect the funding levels requested by the Administration for funding the first five years of the National Airspace System Plan for modernization of the airways system. Committees in both the House and the Senate have held extensive hearings on the National Airspace System Plan, and the conferees are generally supportive of the Plan. However, many aspects of the Plan cannot be developed or analyzed in detail until implementation begins, and in view of the magnitude and complexity of the Plan it is likely that there will have to be adjustments as the Plan is carried out. Clearly, there will be a need for vigorous oversight and monitoring during the implementation of the Plan.

The conferees believe that the requirements imposed by section 504(b) of the Conference Substitute for the formulation and an annual updating of a National Airways System Plan will be especially useful in facilitating Congressional oversight. Section 504(b) requires an annual review, revision, and republication of the Plan at the beginning of each fiscal year. Each Plan must set forth, for a 10-year period, the research, engineering, and development and the facilities and equipment necessary for an airspace system that provides the highest degree of safety in air commerce.

In implementing the National Airspace System Plan, the Conferees expect that the Secretary will ensure that the rules and regulations issued pursuant to Public Law 89-306 (Brooks Act) are strictly adhered to. This Act is founded upon two basic objectives: (1) ADP resources should be procured as economically and efficiently as possible, using full and open competition; and (2) only those resources should be procured which are needed and which can improve the operation of government programs and activities. The Conferees believe these principles to be sound and if followed will greatly increase the likelihood of success of the plan.

The first two years of each Plan will contain detailed annual estimates of the number, type, location, and costs of required facilities and services, costs of R.E.&D. and manpower levels required. The third, fourth, and fifth years of each Plan will contain the estimates of the total cost of each major program for the three-year period and any additional major research program, acquisitions, and manpower changes required to meet the long-range objectives. Finally, each Plan will contain 10-year investment Plan which addressed the long-range objectives for the airway system.

Beyond this comprehensive annual Plan, the Secretary is required to provide the Congress a detailed annual report on the operation of the national airway system during the previous fiscal year and a review of the year's programs intended to improve safety and efficiency of the system. The annual report must include discussions of any significant problems encountered in the program, a summary of funds committed in each major program area, and a report on amounts appropriated but not expended for such programs. The conferees expect these annual reports to address the problems raised by the General Accounting Office in its report, AFMD-82-66, "Examination of the Federal Aviation Administration's Plan for the National Airspace System."

With active and continued oversight by the House and Senate Committees with jurisdiction in this area, supported by the requirements imposed by section 504(b) modernization of the airway system can proceed with a full understanding and justification of the choices and decisions made.

Funds authorized for research, engineering, and development shall be distributed in accordance with:

FAA—5-YEAR FUNDING PROFILE

[In millions of dollars]

	Fiscal year—				
	1983	1984	1985	1986	1987
RE&D/FE&D	133.5	286.0	269.0	215.0	193.0
RE&D	116.7	261.3	245.9	192.3	171.0

FAA—5-YEAR FUNDING PROFILE—Continued

[In millions of dollars]

	Fiscal year—				
	1983	1984	1985	1986	1987
ATC	55.1	77.5	79.3	72.5	94.0
Adv Computer	47.0	156.6	134.5	86.0	46.2
Navigation	5.3	10.5	11.3	10.8	6.4
Weather	8.1	15.4	19.9	22.2	23.6
Medicine	1.2	1.3	.9	.8	.8
FE&D	16.8	24.7	23.1	22.7	22.0
Aircraft safety	13.0	18.4	17.2	17.4	16.5
Medicine	1.8	3.9	3.3	2.7	2.8
Environment	2.0	2.4	2.6	2.6	2.7

Those line items under Facilities Engineering and Development (FE&D) were previously funded from general revenues and are to remain separately identified from Research Engineering and Development (RE&D) which is primarily aimed at accomplishing the National Airspace System (NAS) Plan to modernize the ATC System.

Notwithstanding the purposes for which funds are authorized in the above table, these funds may be used for any other research, development, and demonstration program or project including related or supporting facilities and equipment under section 312(c) of the Federal Aviation Act of 1958 if notice of such program or project has been given to the Speaker of the U.S. House of Representatives; the Committees on Science and Technology, and Appropriations of the U.S. House of Representatives; the President of the Senate; and the Committees on Commerce, Science and Transportation, and Appropriations of the Senate, in a manner containing a full and complete statement of the proposed program or project and the facts and circumstances relied on in support of such program or project, and (1) a period of thirty days has passed after the date such notice was received, or (2) each such Committee has transmitted to the Secretary of Transportation before the expiration of such period written notice that such Committee has no objection to the proposed action.

The Conferees support the intent of the FAA to modernize the Air Traffic Control System through the implementation of the National Airspace System Plan which was produced as directed by the Committee on Science and Technology in H. Res. 202 approved by the House October 19, 1981. Because of the significant technological complexities and costs involved, the Conferees believe it is extremely important that continued oversight be sustained.

In this regard, the Administrator of the Federal Aviation Administration is requested to submit to the House Committee on Science and Technology and the Senate Committee on Commerce, Science and Transportation, not later than April 1, 1983, and annually thereafter, a report that summarizes activities under the NAS program. This should include, but not be limited to, historical data that compares achievements versus plans in terms of productivity, safety, costs, schedules, and milestones. Modifications of the Plan for subsequent year should also be identified.

8. APPORTIONMENT OF FUNDS

Senate amendment:

Provides an apportionment to primary airports based on an enplanement formula that is the same as in existing law. The amount of ADAP funds made available to primary airports is 55 percent in fiscal year 1982 and 50 percent thereafter. The amount apportioned to each primary airport will be increased by 10 percent in fiscal 1984, 20 percent in fiscal 1985, 25 percent in fiscal 1986, and 30 percent in fiscal 1987. The maximum apportionment to a primary airport is $12,500,000. Passenger enplanements are determined for the preceding calendar year.

The second apportionment is to States for airports other than reliever airports, primary airports, and airports that withdraw from the program. Ten percent of ADAP funds are apportioned to States, with one-half of one percent going to insular areas and the remaining 99.5 percent going to the States (including Puerto Rico) according to a population and area formula. Each State is apportioned an additional amount for each of fiscal years 1984 through 1987, increasing from $150,000 to $240,000 per fiscal year.

Amounts remaining in the Trust Fund shall constitute a discretionary fund.

In addition, the Secretary may apportion amounts to airports in the State of Alaska in the same manner as amounts were apportioned for fiscal year 1980.

Conference substitute:

Same as the Senate, except:

(1) There is a cap on apportionments to primary airports of 50 percent.

(2) In addition to the maximum apportionment to a primary airport, there is a minimum apportionment of $200,000 per fiscal year.

(3) The apportionment to States is 12 percent of ADAP funds and is for general aviation and reliever airports. One percent is set aside for insular areas, which may also use the money for nonprimary commercial service airports, and 99 percent for States (including Puerto Rico). The additional apportionment to States under the Senate amendment is not included in the conference substitute.

(4) The provision allowing apportionments to airports in Alaska under the 1970 Act is qualified so that not more than 110 percent of the amount so apportioned to a commercial service airport in Alaska is obligated at that airport during the fiscal year from these apportioned funds. In no event shall any primary airport be apportioned less under this paragraph than it would be apportioned under the section governing primary airport apportionments.

The Conferees are concerned about the effect on the discretionary fund of the naming of specific ADAP or Facilities and Equipment projects in legislation or report language. The ADAP program contemplates that a large proportion of funding be available on a discretionary basis. This is the only way that we will be able to build and implement an integrated system of public use airports while addressing project needs which are too large to fit annual enplanement funds or which are urgently needed for safety. It is also the only way that new airports can normally be funded. Similarly, the F&E program must be administered so that funds will go where the safety needs are greatest.

In recent years, the tendency to name specific projects in committee reports has grown more widespread. These named projects threaten to use up discretionary funds so that there will be no real discretion left. For example, in fiscal year 1981, a total of 38 specific ADAP projects were named in DOT Appropriations legislation. Grants to these airports totaled $43.5 million in fiscal year 1981. This practice has the potential of using up a significant portion of the discretionary fund.

The problem becomes particularly acute with the limited availability of funds for the ADAP and F&E programs. It will not be possible to fund all projects seeking ADAP and F&E grants and it will be necessary for the Secretary to establish priorities to determine which projects should be funded. The Conferees expect the Secretary to establish these priorities solely on the basis of the criteria set forth in the authorizing legislation. Projects which qualify for funding and have a high priority under the statutory criteria should not be denied funding in favor of projects which have a lower priority under the statutory criteria but are mentioned in legislative history. The criteria established by the authorizing legislation should not be construed as being overruled or amended during the life of that authorization by other subsequently enacted legislation or legislative history, unless such legislation specifically and expressly amends the authorizing law to establish new criteria or priorities.

9. MINIMUM FUNDING

Senate amendment:

Establishes minimum levels of funding for the following categories of airports:

(1) reliever airports: 10 percent of ADAP funds during the 6-year period of the bill;

(2) each nonprimary commercial service airport that received Federal assistance for fiscal year 1980, for high priority projects: the amount the airport would have been apportioned under the primary apportionment formula for fiscal years 1983-1987, or five times the airport's 1980 apportionment, whichever is greater; and

(3) airports other than relievers or commercial service airports: $300,000,000 for the 6-year period of the bill.

Conference substitute:

Provides the following minimum levels of funding for each fiscal year of the bill:

(1) reliever airports: 10 percent of ADAP funds made available for obligation;

(2) for noise compatibility planning and carrying out noise compatibility programs: 8 percent of ADAP funds made available for obligation;

(3) nonprimary commercial service airports and certain noncommercial service airports that received Federal assistance during fiscal year 1981: 5.5 percent of ADAP funds made avail-

able for obligation, an amount which does not include apportionments to airports in Alaska; and

(4) for integrated airport system planning: one percent of ADAP funds made available for obligation.

The Secretary is not required to meet these requirements if there are not enough applications to enable the Secretary to obligate the minimum amount required.

With regard to noise compatibility grants, the Conferees recognize the value of public building soundproofing especially where this type of grant aids in the efficiency of certain essential functions such as education.

Of major concern to the conferees is the financial threat to privately-owned relievers in major metropolitan areas. Large hub areas in particular need such aviation facilities to separate commercial and general aviation traffic, but the land is often more valuable if converted to other commercial uses. In such instances it is important that the Federal Government assist local governments in preserving these essential reliever airports. As a result, for the first time, this bill proposes to fund projects at privately-owned public use airports, which may prove sufficient in some instances. In other instances, these reliever funds could be used to assist in the outright purchase of privately owned relievers. For example, such purchase plans have been discussed for airports in the Chicago area, North Las Vegas, Southern California, and other major metropolitan areas. The conferees expect the Administrator to make every effort to accommodate such needs where they are essential to the maintenance of reliever airports.

10. USE OF APPORTIONED FUNDS

Senate amendment:

Provides the "form of obligation" which the Secretary shall use to obligate apportioned funds, either by project grant or block grant.

Amounts apportioned are available for obligation by grant agreement during the fiscal year for which they were first authorized to be obligated and the 2 fiscal years immediately following.

A sponsor of a primary airport is permitted to use funds apportioned to it at any public airport of the sponsor which is in the NASP. A sponsor of a primary airport may also waive receipt of all or a portion of its funds on condition that the funds be used at another public-use airport in the State or geographical area.

Conference substitute:

Same as Senate, except for deletion of references to block grants. Funds apportioned to a State are made available to general aviation and reliever airports in that State.

11. PROJECT GRANTS: APPLICATION; APPROVAL

Senate amendment:

This section provides some of the requirements which must be set forth in an application for a project grant for airport development or airport planning and requirements which must be met by the Secretary of Transportation before approving such project grant applications.

The provision sets forth who is eligible to apply to the Secretary for a project grant for airport development or airport planning with the proviso that no public agency may submit an application if such submission is prohibited by State law.

This section also provides that within 180 days of enactment a sponsor may submit a project-grant application for any project for which either an application had been filed before September 30, 1980, or if the project was carried out after September 30, 1980, and before enactment of this Act.

Each primary airport is to notify the Secretary of the fiscal year in which it intends to apply for apportioned funds.

The section provides conditions which must be met by the Secretary before project applications for airport planning or development may be approved.

Conference substitute:

Essentially the same as the Senate amendment, except that a condition in the Senate amendment that the Secretary not approve a project unless he is satisfied that the project is consistent with the purposes of the title is not included, and two additional provisions are added: (1) a provision that no environmental impact statement is required for a project if it would allow nonstage 2 aircraft to be replaced with stage 2 aircraft at the airport; and (2) a provision that priority may be given to projects that are consistent with integrated airport system plans.

12. U.S. SHARE OF PROJECT COSTS

Senate amendment:

Provides that, generally, the U.S. share of allowable project costs payable on account of any project funded under this Act shall not exceed 90 percent of allowable project costs.

For primary airports enplaning .25 percent or more of the total number of passengers enplaned annually at all commercial service airports, the U.S. share of allowable cost payable shall not exceed 75 percent of allowable project costs. As in existing law, an increased Federal share is provided for projects in those States in which certain public land acreage exceeds 5 percent of the States total area.

Conference substitute:

Same as the Senate amendment, except that instead of stating that the U.S. share shall not exceed a certain percentage, the substitute states that the U.S. share shall be that percentage.

13. SPONSORSHIP REQUIREMENTS FOR PROJECT GRANTS

Senate amendment:

Sets forth requirements which must be met by sponsors before project grant applications may be approved. These continue many of the requirements and provisions of section 16 of existing law for certain nondiscrimination, safety and other reporting requirements for airport sponsors which accept Federal funds. Two new provisions were added. One is that airports receiving assistance under this program must dedicate all revenues generated by the airport for the capital operating costs of that airport, the local airport system, or other local facilities which are owned by the owner or operator of the airport and used for the transportation of passengers or property. This provision is designed to ensure that airport systems which are receiving Federal assistance are utilizing all locally generated revenue for the systems which they operate. Airports that are part of a unified ports authority are exempt from this requirement if covenants or assurances in previously issued debt obligations or controlling statutes require that these funds are available for use at other port facilities.

However, airports users should not be burdened with "hidden taxation" for unrelated municipal services.

This provision is not intended to apply to revenue generated by facilities which are located on airport property but are unrelated to air operations or services which support or facilitate air transportation. It would accordingly not apply to revenue generated by such facilities as a water reservoir or a convention center which happen to be located on airport property, but which serve neither the airport nor any air transportation purpose. It would apply to such facilities as terminal concessions and parking lots serving the terminal or other air transportation purposes.

The language regarding "local facilities which are owned or operated by the owner or operator of the airport and used for the transportation of passengers or property" was included to make clear the intent that the requirement would not prohibit the use of revenues for the purpose of retiring indebtedness on consolidated bonds which have been used in some jurisdictions to finance multimodal transportation facilities which are owned or operated by the owner or operator of an airport and used for transportation of passengers or property but which are not themselves airport facilities.

The second new provision relates to land acquired for noise compatability purposes. It requires that when such land is acquired, the sponsor must, at the earliest possible time, and subject to the retention or reservation of the interest or right necessary to ensure that the land is used only for purposes which are compatible with noise levels of the operation of the airport, use it best efforts to dispose of such land. When such land is disposed of the provision requires that the proceeds of the disposition shall be refunded to the United States for the Trust Fund on a basis proportionate to the U.S. share of the cost of acquisition of the land.

The Senate amendment continues existing provisions of law relating to compliance with sponsorship requirements.

Conference substitute:

Same as the Senate with the following additions:

(1) an assurance that each air carrier using an airport will have the right to service itself or use a fixed-based operator;

(2) an assurance that there will be no exclusive right for the use of an airport by providers of aeronautical services; use of an airport by a single FBO is not to be construed as an exclusive right if it would be unreasonably costly, burdensome, or

impractical for more than one FBO to provide the service, and if allowing more than one FBO would require reduction of the existing FBO's leased space;

This provision shall not be construed to allow an airport operator to enter into a lease agreement with a fixed base operator (FBO) which guarantees such FBO an exclusive right to provide aeronautical services on the airport. In addition, it shall not preclude a new FBO from leasing airport property which is not then subject to an existing lease between an airport operator and another FBO.

(3) proceeds from the disposition of land previously acquired for noise compatibility may be reinvested in an approved project.

14. BLOCK GRANTS TO STATES

Senate amendment:

Permits States to apply to the Secretary to distribute the funds apportioned to that State for airport development.

Conference substitute:

No comparable provision.

15. ACCEPTANCE OF CERTIFICATION; CONSULTATION

Senate amendment:

Requires that the Secretary put a maximum reliance on sponsor certification as a means of administering grants, under the bill.

This section also continues the requirement in existing law that airport operators receiving funds consult with parties using the airport prior to undertaking an airport development project.

Conference substitute:

The substitute continues the requirement that in making a decision to undertake airport development under the Act, a sponsor shall undertake reasonable consultations with affected parties using the airport at which the project is proposed. The FAA has implemented this requirement by publishing in the Airport Development Aid Program Handbook an extensive description of such matters as the time at which consultations should take place, and the scope of consultation required to be meaningful. The FAA's description establishes the type of consultation contemplated by the reported bill and should be continued.

With respect to certification, the Secretary is authorized to require a certification from a sponsor that the sponsor will comply with all requirements imposed by the Act. The substitute provides that nothing in the certification provision affects the Secretary's responsibilities under specified Federal laws.

16. GRANT AGREEMENTS

Senate amendment:

This section outlines the duties of the Secretary and the sponsor of a project when grants are approved. The section provides that unless and until an agreement has been executed, the United States may not pay, or be obligated to pay any portion of the costs which have been or may be incurred in connection with a project. Further, the provision requires that the total obligation of the Federal Government may not exceed the amount specified as the maximum Federal obligation in the grant agreement, except in the case of airport development in which case such amount may be increased by 10 percent and by an additional amount equal to 50 percent of any increase in project cost attributable to land acquisition.

Also provides that increases in the maximum obligation of the United States in the case of grants under the 1970 Act may be paid only from funds recovered by the United States under that Act.

Conference substitute:

Same as the Senate with the clarification that in the case of increased costs attributable to land acquisition, the increase allowed shall be based upon current credible appraisals.

17. PROJECT COSTS

Senate amendment:

Eligible project costs are those associated with carrying out the project, and which are directly connected to the costs of the project. Indirect costs, such as administrative and salary costs, are not permitted to be paid for as a part of the project costs. Costs are eligible if they were incurred after the contract grant agreement was signed and are consistent with the terms of the contract. The act permits funding for the cost of field surveys, preparation of plans and specifications, acquisition of land and other direct costs associated with an airport development or planning project. The Secretary may agree to pay for only those reasonable costs associated with the project. However, the Secretary cannot pay for costs which are in excess of the amount previously agreed to in the contract as the Secretary's share. In the event the Secretary wishes to audit project costs, he is permitted to establish whatever regulations considered necessary to that task.

Terminal development costs are eligible, up to 50 percent of project costs. In the case of a primary airport, not more than 60 percent of the airports apportionment may be used for this purpose, and in the case of a non-primary commercial service airport not more than $200,000 may be used in a fiscal year. These funds can only be approved after all necessary safety, security, passenger enplaning/deplaning facilities, and equipment have been provided at the airport.

Conference substitute:

Same as the Senate except that a primary airport can use the greater of $200,000 or 60 percent of its apportionment for terminal development. In addition a $25,000,000 cap is placed upon terminal development at commercial service airports which were not eligible for terminal development assistance in fiscal year 1980. Third, the prohibition on funding indirect costs is not included. Finally, the substitute includes a provision continuing the eligibility of costs incurred for the retirement of the principal of bonds issued for terminal development work performed between 1970 and 1976.

18. PAYMENTS UNDER GRANT AGREEMENTS

Senate amendment:

Defines the terms under which advance payments may be made to airport sponsors by the Secretary. This closely follows existing law. The time and amount are to be determined by the Secretary with the total amount committed not to exceed 90 percent of the project cost. The sponsor must certify that advance payments will not exceed allowable project costs. If they do, the sponsor must return the excess to the Secretary. If work for the project is not completed within a reasonable time, the Secretary is entitled to reclaim any part of the advance payment.

Conference substitute:

Same as the Senate amendment.

19. PERFORMANCE OF CONSTRUCTION WORK

Senate amendment:

Entitles the Secretary to inspect and approve any construction work accomplished with funds obligated under project grants.

The amendment provides that contracts in excess of $2,000 for work under project grants for airport development approved under the bill which involve labor shall comply with the Davis-Bacon Act. The section further provides that Vietnam era and disabled veterans are to be given preference in hiring (with the exception of executive, administrative and supervisory positions). These priority hiring requirements are only enforceable when such individuals are available and qualified to perform the work to which the employment relates.

Conference substitute:

Same as the Senate amendment.

20. USE OF GOVERNMENT-OWNED LANDS

Senate amendment:

This section closely follows current law. The Secretary is empowered to seek authority from the head of a department or agency having control over certain nonexempted public lands, to turn over to an airport sponsor for the purpose of meeting future airport development needs. The Secretary can reach agreement to transfer the title to, interest in, or an easement of such property or airspace to the airport sponsor. The head of the department or agency must respond to the Secretary's request within 4 months with a decision. If a determination is made that the title to or use of the land by the airport is not inconsistent with the needs of the department or agency, the land can be turned over, with the approval of the U.S. Attorney General, and without cost to the United States.

As in the existing Act, these lands may not include any U.S. owned or controlled national park, forest, monument, recreation area, or other area administered by the National Park Service, the National Wildlife Refuge System, or the Bureau of Sport Fisheries and Wildlife. This exemption also includes Indian reservations.

Conference substitute:

Same as the Senate amendment.

21. FALSE STATEMENTS

Senate amendment:

This section duplicates section 25 of the present law. It allows for the imprisonment of up to 5 years, or a fine of up to $10,000, or both, for any person who attempts to willfully defraud the United States, by making false statements or representations with respect to the cost, quality, or quantity of material provided in connection with an airport project constructed with Federal funds.

Conference substitute:

Same as the Senate.

22. ACCESS TO RECORDS

Senate amendment:

This section imposes the same requirements as section 26 of the existing law. Grant recipients are required to keep detailed and complete accounts of all costs and work performed in connection with an airport project in order to facilitate an effective audit.

The Secretary may establish recordkeeping requirements which are considered necessary to ensure an effective audit, and these requirements must be reviewed annually. The Secretary and the Comptroller General of the United States are given authority to examine and audit any records or papers pertinent to grants under the bill.

In the case where an independent audit is performed in association with a Federal project, a certified copy of the audit must be filed with the Comptroller General of the United States within 6 months after the close of the fiscal year in which the audit was made. The Comptroller must make annual reports to Congress on or before April 15 each year with the results of these audits.

Congress is to have access to all information made available to the Secretary and the Comptroller General.

Conference substitute:

Same as the Senate amendment.

23. GENERAL POWERS

Senate amendment:

This section gives the Secretary General authority to conduct public hearings, investigations and institute those regulations and procedures which he considers necessary to perform his duties under the bill. This duplicates section 27 of existing law.

Conference substitute:

Same as the Senate amendment.

24. CIVIL RIGHTS

Senate amendment:

This section gives the Secretary authority to promulgate regulations to ensure that no person is discriminated against on the basis of race, creed, color, national origin, or sex in connection with the work on a project supported by Federal funds released pursuant to the bill. This language tracks that of section 30 in the present law and is a responsibility in addition to those obligations set out in title VI of the Civil Rights Act of 1964.

Conference substitute:

Same as Senate amendment.

25. JUDICIAL ENFORCEMENT

Senate amendment:

This section is new and would make clear that the Secretary, acting through the Attorney General, has the right to obtain judicial enforcement against persons who violate the provisions of the bill or the rules, regulations, requirements, or orders issued pursuant thereto.

Conference substitute:

No comparable provision.

This action in no way affects any rights which the Department of Transportation may have to judicial enforcement.

26. VOLUNTARY WITHDRAWAL FROM PROGRAM

Senate amendment:

This section permits any airport to elect not to receive airport development funds. If an airport chooses to defederalize, it remains eligible for Federal assistance for land acquisition and noise abatement.

The provision requires the Secretary of Transportation to conduct a study on whether, and to what extent, those airports which have the ability to finance their capital and operating needs without Federal assistance should remain eligible for airport development funds. The report must be submitted to Congress no later than one year from enactment of this bill. The study must review how a defederalization program might work and how a passenger facility charge might be imposed.

Conference substitute:

The conference substitute retains only the study and report requirements.

27. WAIVER OF OBLIGATIONS

Senate amendment:

This section directs the Secretary to issue procedures pursuant to which airports which no longer receive airport development funds may exercise the airport's option to terminate existing assurances, requirements or contractual obligations that are tied to the acceptance of these funds.

Conference substitute:

No comparable provision.

28. REPEALS; EFFECTIVE DATE; SAVINGS PROVISIONS; SEPARABILITY

Senate amendment:

This section specifies that the effective date of the bill is its date of enactment and that on that date sections 1 through 31 of the Airport and Airway Development Act of 1970 are repealed. It also includes a savings provision to permit certain sections of the 1970 Act to continue in effect under the new bill, including one directed to keeping amounts apportioned before October 1, 1980, available for obligation.

Conference substitute:

Same as the Senate amendment, except that sections 1 through 30 of the 1970 Act are repealed.

29. REPORT TO CONGRESS ON TRUST FUND

Senate amendment:

This section modifies a provision in the existing law which requires an annual report to Congress on operations under the Airport and Airway Development Act of 1970 to require only a simple financial statement itemizing the income, obligations, expenditures, and uncommitted balance in the Airport and Airway Trust Fund.

Conference substitute:

Continues the existing annual report.

30. STANDARDS FOR RUNWAY FRICTION

Senate amendment:

This section amends section 612 of the Federal Aviation Act of 1958 regarding airport operating certificates. In section 612 the Administrator of the Federal Aviation Administration is directed to impose on certificated airports such conditions and limitations as are determined to be necessary to insure safety in air transportation. This amendment would add grooving and other friction treatment of primary and secondary runways as an item to be considered by the Secretary in making this determination.

Conference substitute:

Same as the Senate amendment.

31. EQUAL AERONAUTICAL ACCESS

Senate amendment:

This section of the bill amends section 308 of the Federal Aviation Act of 1958 (49 U.S.C. 1349) to continue the same standard of access at any federally assisted airport that exists in current law. The language of the provision is modeled after that which is contained in existing sponsorship agreements now used by Secretary of Transportation in awarding grants-in-aid to federally assisted airports.

Conference substitute:

Deletes Senate provision but adds another provision relating to the exclusive right of use issue, to say that the providing of services at an airport by a single fixed-based operator (FBO) shall not be construed as an exclusive right if it would be unreasonably costly, burdensome, or impractical for more than one FBO to provide the services and if it would require a reduction in the existing FBO's leased space.

32. CONFORMING AMENDMENTS

Senate amendment:

This section provides clarification of definitions for the Aviation Safety and Noise Abatement Act of 1979.

Conference substitute:

Contains additional conforming amendments to the Aviation Safety and Noise Abatement Act of 1979 and technical amendments to other laws.

33. SECURITY SCREENING IN FOREIGN AIR COMMERCE

Senate amendment:

This section extends through fiscal year 1982 existing law that authorizes an appropriation for unreimbursed security costs in international air transportation. Any appropriation made under this section is limited to not more than $9.75 million. The Secretary of Transportation is required to submit a recommendation to the Congress on amounts due specific air carriers under this section.

Conference substitute:

The conference substitute authorizes appropriations of $15 million for reimbursement of security costs. Compensation is to be provided only with respect to amounts expended on or before the 180th day after the date of enactment of the International Air Transportation Competition Act of 1979.

34. SAFETY CERTIFICATION OF AIRPORTS

Senate amendment:

Under current law, the authority of the Administrator of the Federal Aviation Administration to issue airport operating certificates is limited to airports that are served by air carriers certificated by the Civil Aeronautics Board (CAB). This section substitutes a new standard for airport certification based upon the number of revenue passengers enplaned (2,500 per year) or the size of air carrier aircraft using the facility (more than 30 passenger seats).

Conference substitute:

Same as the Senate amendment except that the only standard for airport certification is the one based on size of aircraft (more than 30 passenger seats).

35. PART-TIME OPERATION OF FLIGHT SERVICE STATIONS

Senate amendment:

The purpose of this provision is to limit the number of Flight Service Stations which may be part-timed or closed from the date of enactment until September 30, 1983, and to provide certain standards for their closure or part-timing thereafter.

Conference substitute:

Essentially the same as the Senate amendment.

36. CONGRESSIONAL COMMITTEES

Senate amendment:

This section provides that nothing in the Act shall be construed as altering the jurisdiction of the Senate Commerce Committee or the House Public Works Committee over the Airport and Airway Development Program.

Conference substitute:

No comparable provision.

37. CONTRACTING AUTHORITY

Senate amendment:

No provision

Conference substitute:

This section provides that in contracting out for the operation of any airport facility by any State or political subdivision thereof, the Secretary of Transportation is to assure that any contract, lease, or other agreement by which the State or political subdivision would undertake the responsibility for operating an airport facility must contain a provision holding the United States Government harmless from liability for acts or omissions of an employee or agent of the State or subdivision. Thus, for example, the U.S. Government could not be held liable for the action of an employee or agent of a State or political subdivision who has negligently provided air traffic control services which result in an aircraft accident or incident. On the other hand, to the extent an employee or agent of such State or political subdivision was strictly following F.A.A. procedures and the procedures were determined to be at fault rather than their application, the provisions of established tort law applicable to liability of the United States would be undisturbed by this section.

The Farmington, New Mexico, control tower is illustrative of the application of this provision. The control tower is now staffed and operated by private air traffic controllers at approximately half the costs associated with F.A.A. personnel. On October 1, 1982, the F.A.A. plans to staff the tower with F.A.A. controllers for 16 hours a day, 7 days a week, which are the hours of operation under existing contracted services. This provision provides the authority for the City of Farmington to continue the operations of the control tower by private controllers and maintain overall continuity. With the use of F.A.A. funds to pay the costs associated with contracted air traffic control services, the heavy burden of financially supporting the control tower is removed from the City of Farmington.

The Conferees expect that before contracting out for the operation of airport facilities by any State or political subdivision, the F.A.A. will assure that such locality will fully comply with all applicable safety regulations in their operation of such facilities.

38. STUDY OF AIRPORT ACCESS

Senate amendment:

No provision.

Conference substitute:

Provides that the Secretary shall appoint a Task Force of specified government agencies and aviation groups to study the problem of allocating the use of airport facilities and airspace. The Chairman of the Task Force shall be the Chairman of the Civil Aeronautics Board. The Task Force shall begin meeting not later than 90 days after enactment and shall complete its study not later than 120 days after the Task Force first meets.

39. K-9 TEAMS

Senate amendment:

No provision.

Conference substitute:

Authorizes the Secretary of Transportation to continue the Explosive Detection K-9 Team Training Program for fiscal years 1981-1987 at an authorized level from the Trust Fund of $130,000 to $150,000 per fiscal year.

40. RELEASE OF CERTAIN DEED RESTRICTIONS

Senate amendment:

No provision.

Conference substitute:

Contains standard provisions giving the Secretary of Transportation authority to grant releases from deed restrictions to four airports: Crystal City, Texas; Brownwood, Texas; Grand Junction, Colorado; and Newport, Arkansas.

41. CONTINUATION OF CERTAIN CERTIFICATES

Senate amendment:

No provision.

Conference substitute:

Extends for 2 years beyond the date of expiration any certificate issued under section 401(d)(8) of the Federal Aviation Act of 1958, pursuant to the Trans-Atlantic Route Proceeding, or in the California/Southwest-Mexico Route Proceeding.

42. STATE TAXATION

Senate amendment:

No provision.

Conference substitute:

This section provides that States may not tax at a level which unreasonably burdens or discriminates against interstate commerce. The provision makes current law which prohibits the assessment, levying, or collecting of taxes on motor carrier property in a manner different from that of other commercial and industrial property, applicable to air carriers.

Committee on Ways and Means for the entire bill and the Senate amendment and modifications committed to conference, with the exception of subtitle B (Medicaid) of title I and title IV (Airport and Airway System Development) except for section 406(e) of that title and with the exception of section 395 of the Senate amendment and modifications committed to conference:

Dan Rostenkowski,
Sam Gibbons,
J. J. Pickle,
Charles B. Rangel,
Pete Stark,
Barber B. Conable, Jr.,

Committee on Energy and Commerce solely for the consideration of subtitle B of title I (Medicaid), of the Senate amendment and modifications committed to conference and subtitle C of title I (Utilization and Quality Control Peer Review) of the Senate amendment and the modifications committed to conference and such parts of subtitle A (Medicare) of title I of the Senate Amendment and modifications committed to conference that relate to amendments to the supplementary medical insurance program authorized under title XVIII of the Social Security Act:

John D. Dingell,
Henry A. Waxman,
James H. Scheuer,
Jim Broyhill,
Ed Madigan,

Committee on Energy and Commerce solely for consideration of section 395 of the Senate amendment and modifications committed to conference:

John D. Dingell,
Timothy E. Wirth,
James T. Broyhill,

Committee on Public Works and Transportation solely for the consideration of title IV of the Senate amendment and modifications committed to conference with the exception of sections 406(e) and 407(b) of that title:

NORMAN Y. MINETA,
GLENN M. ANDERSON,
ELLIOTT H. LEVITAS,
JAMES L. OBERSTAR,
DON CLAUSEN,
GENE SNYDER,
JOHN PAUL HAMMERSCHMIDT,

Solely for the consideration of section 407(b) of title IV of the Senate amendment and modifications committed to conference:

DON FUQUA,
DAN GLICKMAN,
LARRY WINN, Jr.,
Managers on the Part of the House.

For the entire bill with the exception of title IV (airport and airway system development) except for section 406(e)):

BOB DOLE,
BOB PACKWOOD,
BILL ROTH,
JOHN C. DANFORTH,
RUSSELL B. LONG,
LLOYD BENTSEN,

Solely for consideration of title IV (excluding section 406(e)):

BOB PACKWOOD,
NANCY LANDON KASSEBAUM,
HOWARD W. CANNON,
Managers on the Part of the Senate.